

COM/CJS/jt2

**PROPOSED DECISION**

Agenda ID #13488 [\(Rev. 1\)](#)

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[12/18/2014 Item #66](#)

Decision **PROPOSED DECISION OF COMMISSIONER SANDOVAL**

(Mailed 11/17/2014)

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

Order Instituting Rulemaking into the Review  
of the California High Cost Fund-A Program.

Rulemaking 11-11-007  
(Filed November 10, 2011)

**DECISION ADOPTING RULES AND REGULATIONS IN PHASE 1 OF THE  
RULEMAKING FOR THE CALIFORNIA HIGH COST FUND-A PROGRAM**

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**DECISION ADOPTING RULES AND REGULATIONS IN PHASE 1 OF THE RULEMAKING FOR THE CALIFORNIA HIGH COST FUND-A PROGRAM****Summary**

This decision adopts rules and regulations in Phase 1 of the Rulemaking 11-11-007 (OIR) in the California High Cost Fund-A Program (CHCF-A or the A-Fund). The A-Fund is available for telecommunications services provided by 13 rural telephone corporations (or Rural Local Exchange Carriers (RLECs)) in California.<sup>1</sup> A primary goal of the OIR is for the Commission to determine how the CHCF-A program can more efficiently and effectively meet its stated goals of providing affordable, widely available, safe, reliable and high quality communications services for rural areas of the state.

Thus, this proceeding examines the appropriate regulatory framework to ensure the continued provision of safe, reliable telecommunications services to rural areas at just and reasonable rates. In examining this framework, the Commission seeks to balance investments from the High Cost Funds with appropriate contributions from RLEC customers, and maximize federal funding to leverage federal, state, and customer dollars to ensure high-quality service.

The areas California RLECs serve are characterized by high costs, less dense populations than urban or suburban areas, with many serving in areas

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<sup>1</sup> The RLECs include Calaveras Telephone Company, Cal-Ore Telephone Company, Ducor Telephone Company, Foresthill Telephone Company, Happy Valley Telephone Company (Happy Valley); Hornitos Telephone Company (Hornitos); Kerman Telephone Company, Pinnacles Telephone Company, The Ponderosa Telephone Company, Sierra Telephone Company, Inc., The Siskiyou Telephone Company and Volcano Telephone Company and Winterhaven Telephone Company (Winterhaven). Happy Valley, Hornitos, and Winterhaven are eligible for A-Fund subsidies but currently do not draw from the A-Fund. The remaining 10 RLECs that do draw on the A-Fund are known as the Independent Local Exchange Carriers (Small ILECs).

where the terrain increases deployment and maintenance costs. Speakers at the Public Participation Hearings reported that cell service was spotty in many areas the RLECs serve, and in some places not available at all. Terrain and weather challenges add to network deployment costs and affect the ability of customers to use other communications technologies such as wireless and satellite.

Ensuring that RLEC subscribers have reliable communications services that support robust broadband furthers the universal service goals of state and federal statutes. Such service increases economic opportunities for people in rural areas and improves the state's economy as a whole as communication with rural areas becomes more accessible. High quality, reliable communications facilities and service enhances public safety in rural areas, many of which are classified as high wildfire danger regions, and therefore throughout the state as a whole.

In ~~2012~~2012, the California Legislature passed Senate Bill 379 which is codified as Section 275.6 of the Public Utilities (Pub. Util.) Code. Among other things, Section 275.6 allows these RLECs to include all reasonable investments necessary to provide for the delivery of high-quality ~~communication~~communications services , including the deployment of broadband-capable facilities in their rate base.<sup>2</sup>

As technology and consumer demand have changed, so too have the networks used to provide telecommunications services, including those that serve California's rural areas. Many networks are a hybrid of copper and fiber, and broadband-capable networks offer both broadband Internet service and telephone service. In light of the statutory mandate of Section 275.6 to include all

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<sup>2</sup> Pub. Util. Code § 275.6.

RLEC investments for broadband-capable networks in rate base, and to meet the universal service, reliability, public safety, and just and reasonable rate statutory mandates, this Decision takes steps to promote investment in broadband-capable networks, and balance impacts on the A-Fund by tailoring customer contributions to more closely reflect urban counterpart rates, and by limiting fund reimbursement for certain RLEC corporate expenses, consistent with recent changes to federal High Cost programs.

## **1. Background and Procedural History**

With the Order Instituting Rulemaking (OIR) ([Rulemaking \(R.\) 11-11-007](#)), the Commission began a review of the California High Cost Fund-A (CHCF-A) program. The OIR was issued pursuant to the Commission's Decision (D.) 10-02-016. The Commission has determined that a detailed review of the program is warranted in response to market, regulatory, and technological changes since the California High Cost Fund program was first established in 1987. In this OIR, the Commission seeks comment on how the program can more efficiently and effectively meet its stated goals. To the extent deficiencies are identified, the Commission will solicit proposals on how the program should be modified consistent with its statutory purposes.

The OIR was approved on November 10, 2011, and issued on November 18, 2011. The preliminary schedule mandated that the initial comments be filed and served 61 days after issuance (January 18, 2012), and that reply comments be due 91 days after issuance. On January 3, 2012 (via e-mail), The Utility Reform Network (TURN), a party in the proceeding, requested an extension of time to file initial comments pursuant to Rule 16.6. In a ruling issued on January 17, 2012, the request for extension was granted. By that ruling the proceeding schedule was

revised so that initial comments were to be filed and served by February 1, 2012, and reply comments were to be filed and served by March 2, 2012.

On February 17, 2012 (via e-mail), the Commission's Division of Ratepayer Advocates ~~(DRA)~~ requested an extension of time to file reply comments. In a ruling issued on February 23, 2012, an extension, allowing reply comments to be filed and served on March 16, 2012, was granted.

On March 8, 2012, Calaveras Telephone Company, Cal-Ore Telephone Company, Ducor Telephone Company, Foresthill Telephone Company, Kerman Telephone Company, Pinnacles Telephone Company, The Ponderosa Telephone Company, Sierra Telephone Company, Inc., The Siskiyou Telephone Company and Volcano Telephone Company (collectively, Small Independent Local Exchange Carriers or Small ILECs) filed a Motion to Disqualify Current Carrier Oversight and Programs Branch Advisors from Further Advisory Roles in the instant proceeding (Motion to Disqualify). Contemporaneously, the Small ILECs filed a Motion to Strike the Opening Comments of Tyler Werrin (Motion to Strike). Attached to the motion was the Declaration of Patrick Rosvall (Rosvall Declaration), counsel for the Small ILECs. Also on March 8, the Small ILECs sent a letter to Commission President Michael R. Peevey requesting that the Commission initiate an investigation into the Communications Division's (CD) conduct in connection with the instant proceeding (Request for Investigation). On March 9, 2012, the Small ILECs filed a Motion to Hold the Proceeding in Abeyance or Extend Time for Reply Comments (Motion to Hold in Abeyance).

On June 4, 2012, a Prehearing Conference (PHC) was held in the instant proceeding. The assigned Commissioner and the assigned Administrative Law Judge (ALJ) were both present at the hearing. The parties discussed how the OIR

should proceed, including the possible need for hearings and/or workshops,<sup>3</sup> as well as the need to clearly define the issues at play.

On June 29, 2012, the assigned ALJ issued a ruling denying the motion to disqualify current Carrier Oversight and Programs Branch advisors from further advisory roles in this proceeding, denying the motion to strike the opening comments of Tyler Werrin and affirming the ruling denying motion to hold proceeding in abeyance. The comments of Tyler Werrin were submitted to the Commission but were never officially filed or entered into the record.

On October 15, 2012, the Small ILECs filed a motion for a Proposed Decision adopting a one-year stay in the ~~California High-Cost Fund A (CHCF-A)~~ General Rate Case Schedule (GRC) and “Waterfall Mechanism.”<sup>4</sup> Various parties filed Responses on October 30, 2012. The Small ILECs filed a Reply to the Responses, on November 5, 2012. On January 11, 2013, Commissioner Sandoval issued a Proposed Interim Decision (PD) adopting a one-year stay in the GRC Schedule of the Small ILECs with the exception of Kerman Telephone Company and a one-year freeze in the Waterfall Mechanism.<sup>5</sup> The PD also allowed the stay and freeze to be extended for six months by the assigned ALJ. Various parties filed initial comments on January 31, 2013, and reply comments on February 5,

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<sup>3</sup> PHC Transcript, 17:12-28, 19:15-28, 21:17-28.

<sup>4</sup> A “Waterfall Mechanism” is a six-year cycle that begins on January 1 after a GRC decision is issued. A company receives full (100%) funding for three years following the GRC decision. In the fourth year the company receives funding at 80% of the GRC decision; in the fifth year 50% and in the sixth year 0%, unless a new rate case is filed. The cycle begins again with the filing and approval of a GRC application.

<sup>5</sup> Retroactive to January 1, 2013 and extending to December 31, 2013.



2013. The Commission adopted the Interim Decision<sup>6</sup> on February 13, 2013. On March 22, 2013, the Small ILECs filed an Application for Rehearing.

On May 22, 2013, the assigned Commissioner issued a Scoping Memo and Ruling. Parties were instructed to file and serve additional comments by June 28, 2013, with reply comments filed and served by July 11, 2013. Parties were instructed to request evidentiary hearings, if necessary, within ten days after reply comments were due. Later, an extension of time was granted by the ALJ, allowing for submission of the additional reply comments on August 16, 2013.

On July 19, 2013, the California Cable & Telecommunications Association (CCTA), TURN, the Office of Ratepayer Advocates (ORA),<sup>7</sup> Happy Valley Telephone Company, Hornitos Telephone Company, and Winterhaven Telephone Company (collectively, TDS Telecom), and the Small ILECs filed reply comments on the Scoping Memo and Ruling.

On August 16, 2013, ORA, TDS Telecom, TURN, and the Small ILECs submitted additional reply comments on the Scoping Memo Ruling.

On August 30, 2013, the Small ILECs submitted a Motion for Evidentiary Hearings (EH). On September 16, 2013, ORA, TURN, and CCTA filed responses to the Small ~~LECs~~ILECs' motion. The Small ~~LECs~~ILECs submitted a Reply to the Responses on September 25, 2013.

On October 24, 2013, the Small ILECs and ORA submitted a Joint Motion for a limited extension of the GRC schedules and a freeze of the waterfall

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<sup>6</sup> D.13-02-005.

<sup>7</sup> The Office of Ratepayer Advocates was formerly known as the Division of Ratepayer Advocates (~~DRA~~). See Stats. 2013, Ch. 356, Sec. 42.

mechanism for CHCF-A recipients. On December 20, 2013, in an ALJ Ruling issued by the assigned ALJ, the requests in the Joint Motion were approved.

On January 27, 2014, the Small ILECs submitted their Motion for Revisions to Scoping Memo, Inclusion of all Material Factual Disputes in EH, and Establishment of Schedule for Phase 1 of this proceeding. On February 11, 2014, TDS Telecom and TURN responded to this Motion. ORA's response followed on February 13, 2014. The Small LECs issued a reply to the responses on February 20, 2014.

On February 25, 2014, ALJ Colbert issued a Ruling Noticing Public Participation Hearings, which scheduled three public participation hearings (PPHs). On February 27, 2014, the Commission issued an Order Denying Rehearing of Decision 13-02-005.

On March 18, 2014, the assigned Commissioner issued an Amended Scoping Memo and Ruling. The Amended Scoping Ruling revised the scope set forth in that earlier Scoping Memo, identified new issues, set forth the issues to be addressed in workshops, EH and/or briefs, and sought additional comments from the Parties, in light of the initial opening comments, the initial PHC, the second PHC, as well as the passage of Senate Bill (SB) 379. In addition, the proceeding was divided into two phases (Phase 1 and Phase 2). On March 25, 2014, the assigned ALJ issued an e-mail ruling clarifying the scope of the comments to the Amended Scoping Ruling. On April 8, 2014, parties filed their initial comments.

On April 9, 2014, a third PHC was held in order to discuss the scheduling and details for workshops, EHs and briefs in the proceeding. Commissioner Sandoval and ALJ Colbert co-presided. On April 17, 2014, a PPH was held in

North Fork, California. On April 21 a PPH was held in Jackson, California. The third and last PPH was held in Yreka, California on May 8, 2014.

On April 15, 2014, the Small ILECs submitted a letter to the Commission's Executive Director pursuant to Rule 16.6 requesting a 60-day extension to the current rate case deadline and associated waterfall mechanism. This deadline, as governed by D.91-09-042, D.13-02-005, and the December 20, 2013 ALJ Ruling issued in R.11-11-007, was set to expire on June 30, 2014. The Commission's Executive Director granted the request on April 29, 2014, effectively extending the rate case deadline and associated waterfall mechanism to August 29, 2014. This extension allowed time for the assigned Commissioner and ALJ to evaluate a proposal for a formal extension of the deadline and issue an appropriate Proposed Decision for the Commission's consideration.

On April 22, 2014, Parties, with the exception of the Small ILECs, filed reply comments to the Amended Scoping Ruling. On April 23, the Small ILECs were allowed to late-file their comments. On May 14, the assigned Commissioner and ALJ issued a Joint Ruling Setting the Scope, Schedule, Procedures and Issues for Phase 1 of the Rulemaking.

A workshop was held on May 28, 2014, where Parties discussed the issues to be addressed as set forth in the Amended Scoping Memo.<sup>8</sup> A workshop report was not filed.

On July 15, 2014, Commissioner Sandoval issued a PD that extended the current stay of the ~~general rate case~~GRC schedules and freeze of the waterfall provisions for CHCF-A recipients adopted in D.13-02-005 on February 13, 2013.

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<sup>8</sup> Amended Scoping Memo and Ruling at 10-12.

The current stay of the GRC schedules and freeze of the waterfall provisions for CHCF-A recipients, set to expire on August 29, 2014,<sup>9</sup> were extended. The stay of the GRC schedules was extended until December 31, 2014. The freeze of the waterfall provisions for CHCF-A recipients was extended to April 2015. The PD allowed for stay of the GRC schedules to be extended for three months by a ruling of the assigned ALJ if Phase 1 of this proceeding is not completed by December 31, 2014. The PD was adopted by the Commission on August 14, 2014.<sup>10</sup>

EHs were held on September 2 through September 4, 2014. Parties filed opening briefs on September 26, 2014 and reply briefs on October 10, 2014.

## **2. Scope of Proceeding**

The current scope of this proceeding adopts and incorporates portions of the scoping proposals set forth in the initial OIR as well as through supplemental briefings, motions, and comments of the parties. There are eight primary issues for Phase 1. We have solicited input from the parties on each of these main issues via hearings, briefs, and/or workshops. The main issues were contained in section 3 of Amended Scoping Memo and were numbered 3.1-3.8. In the instant decision we simply refer to them as issues 1-8 (removing the leading #3). The issues are as follows:

### **1. Should the Broadband Revenues or Profits Count Towards the Intrastate Revenue Requirement?**

#### **(A) Should the Broadband Revenues or Profits Count Towards the Intrastate Revenue Requirement?**

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<sup>9</sup> On April 29, 2014, the Commission's Executive Director granted a request for a 60-day extension of the general rate case deadline.

<sup>10</sup> See D.14-08-010.

- (B) Can and should the Commission standardize costs in considering the Small ILEC's revenue requirement?
- (C) Waterfall Adjustment Issues
- 2. Should the Small ILEC Territory Be Opened to Wireline Competition?**
  - (A) Can and should the Commission open Small ILEC territories to wireline CLEC competition?
- 3. How Should the Commission Account for Federal Subsidy Changes?**
  - (A) Relationship with federal funding: can and should the Commission modify the mechanism for adjusting CHCF-A based on changes in federal funding and/or implementing changes in federal policy?
- 4 What Metrics Should Be Used to Develop Basic Rates?**
  - (A) Proposals to establish metrics for basic service rates.
  - (B) How should basic rates be determined if parties agree that rates can no longer be based on AT&T rates?
- 5. Are Additional Safeguards Needed to Evaluate Investments in Broadband Capable Facilities to Ensure They Are Reasonable?**
  - (A) Should California Public Utilities Commission (CPUC) determine how much of the investment costs may be recovered through Small ILECS from ratepayers for high quality voice communication and the deployment of broadband capable facilities?
  - (B) What standards should be used to evaluate investment in broadband capable facilities?
- 6. Proposals to Establish "Fair-Market Rates" for Affiliate Use of Regulated Networks**
  - (A) Proposal to establish "fair-market rates" for affiliated use of regulated networks.
  - (B) Should adjustments be made to affiliate transaction rules for the Small ILECs?

**7. Changes to Procedural Rules**

- (A) Are changes needed to the procedural rules surrounding CHCF-A which would render the program more efficient?

**8. California Public Utilities Code Issues**

- (A) What is the impact of Section 710 on A-fund carrier regulatory obligations?
- (B) Should A-Fund carriers receive subsidy money if they change basic service offerings to rely on IP-Enabled technologies? What is the appropriate relationship between ~~section~~[Section](#) 275.6 and ~~section~~[Section](#) 710 of the Public Utilities Code?

Due to the complexity of this proceeding, a second phase will be required. In Phase 2, the following issues will be addressed: (1) the applicability of rate of return as a regulatory framework for California's rural ILECs and the operation of the A-Fund; (2) alternative forms of regulation, including whether to introduce incentive based regulation; (3) whether or not to continue the GRC process for the Small ILECs; (4) whether an evaluation of the presence of competition should include all technologies; and (5) proposals to disqualify non-CHCF-A recipients from CHCF-A eligibility; 6) a review of our preliminary conclusion not to open the areas the Small ILECs serve to competition, informed by studies the CPUC will conduct in Phase II on deployment of Broadband Networks and Universal Service, as described in more detail herein; 7) a review of whether imputation of broadband revenues is appropriate for GRC cycles following the first cycle approved after this Decision.

We will now address the issues, comments and our conclusions for the eight issues in Phase 1 of the proceeding.

**2.1. Should Broadband Revenues or Profits Count Towards the Intrastate Revenue Requirement?**

Issue 1 consists of three sub-issues: (A) Should the Broadband Revenues or Profits Count Towards the Intrastate Revenue Requirement?; (B) Can and should the Commission standardize costs in considering the Small ILEC's revenue requirement?; and (C) Waterfall Adjustment Issues.

**2.1.1. ~~A.~~ Should the Broadband Revenues or Profits Count Towards the Intrastate Revenue Requirement**

In 2012 the California Legislature passed SB 379 which is codified Section 275.6 of the Public Utilities Code. Section 275.6 allows the Small ILECs to include all reasonable investments necessary to provide for the delivery of high-quality communication services and the deployment of broadband-capable facilities in their rate base.<sup>11</sup> Many of the Small ILECs have wholly owned unregulated affiliates, Internet Service Providers (ISP), which provide a variety of broadband services. Other Small ILECs have internal divisions provisioning broadband to their rate-base. At issue is whether revenues from these broadband affiliates or operations should be "imputed" to carriers that are subsidized by the CHCF-A when a carrier's revenue requirement is established in GRC proceedings and the amount of A-Fund subsidy is determined.

**2.1.1.1. Comments on the Rulemaking**

In their summary of this issue the Small ILECs state that the Commission cannot and should not incorporate broadband revenues or profits into intrastate

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<sup>11</sup> Pub. Util. Code § 275.6.

ratemaking. They contend that doing so would violate state and federal law, harm consumers, upset the incentives for small, rural carriers to deploy broadband, and harm California's universal service and broadband objectives.<sup>12</sup> The Small ILECs argue that both federal and state authorities make clear that the Commission does not regulate retail ISP services, so to the extent that a broadband imputation proposal would impose requirements on retail ISP affiliates, it would be unlawful. The Small ILECs assert that Federal law binds the Commission to treat Internet access service provided to end-users as categorically unregulated, so the revenues derived from that service are beyond the Commission's jurisdiction.<sup>13</sup> They similarly argue that State law mirrors the federal determination not to apply common carrier regulations to providers of information services. The Small ILECs claim that the Commission has no jurisdiction over ISP affiliates, as they are neither "telephone corporations" nor otherwise included in the definition of "public utility" under the Public Utilities Code, ~~citing~~ Code Section 216 and Section ~~234 of the Code.~~234. The Small ILECs assert that to be a "telephone corporation" a corporation must "own, control, operate, or manage" a "telephone line," and none of the ISP affiliates are engaged in any of these activities.<sup>14</sup> The Small ILECs also argue that broadband imputation would constitute a violation of the U.S. and California Constitutions as taking of property without just compensation.<sup>15</sup>

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<sup>12</sup> Small ILECs Opening Brief, Summary.

<sup>13</sup> *Id.*, 14:14-18.

<sup>14</sup> *Id.*, 15:20-26.

<sup>15</sup> *Id.*, 20:15-25.



The Small ILECs further argue that “plain language” of Public Utilities Code Section 275.6 cannot be reasonably read to support the notion of broadband imputation. The Small ILECs claim that TURN and ORA have taken different approaches to this question and that both approaches are wrong. They state that TURN’s claim that Public Utilities Code Section 275.6 requires broadband imputation lacks explicit statutory language support.<sup>16</sup> The Small ILECs acknowledge that while ORA does not claim that section 275.6 “mandates” imputation, ORA nevertheless mistakenly concludes that imputation does not conflict with the statute.<sup>17</sup> The Small ILECs argue that if the Legislature had intended to effectuate such a fundamental change in the manner in which ratemaking is handled for "small independent telephone corporations," it would have plainly said so in Section 275.6.<sup>18</sup> The Small ILECs state that other provisions of the Public Utilities Code prove that the Legislature does not rely on ambiguous or generalized directives when authorizing the Commission to consider unregulated revenues in ratemaking.<sup>19</sup>

The Small ILECs contend that broadband imputation would be an extraordinarily damaging public policy.<sup>20</sup> The Small ILECs state that while it is probable that broadband imputation would reduce draws on CHCF-A in the short run, those reductions would come at the expense of service reductions and unavoidable price increases for customers in the rural areas served by Small

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<sup>16</sup> Small ILECs Opening Brief, 26:4-7 citing EH Transcript, 720:20-23.

<sup>17</sup> *Id.*, 26:8-11.

<sup>18</sup> *Id.*, 29:14-17.

<sup>19</sup> *Id.*, 30:6-9.

<sup>20</sup> *Id.*, 54:17:19.

ILECs. The Small ILECs contend that, on balance, the benefits of saving statewide CHCF-A contributors a few cents per year cannot outweigh the tangible and immediate detriments to universal service that their customers would experience from broadband imputation.<sup>21</sup> They stand by their testimony, that they say, demonstrates that the companies would have to increase prices and or reduce service quality or availability to remain profitable should broadband revenues be imputed.<sup>22</sup> The Small ILECS argue that for some companies, the consequences of broadband imputation could be even more dramatic than price increases and reduced technical support or service availability. The Small ILECS contend that broadband imputation would strip investors of any meaningful incentive to operate an ISP, and some companies may ultimately close their doors.<sup>23</sup>

The Small ILECs reject the notion that their ISP affiliates are receiving a "free ride" from the small independent telephone corporations by sharing physical plant. The Small ILECs clarify that the "ride" in question is the local loop. While TURN and ORA both assert that the ISP affiliates unfairly benefit from access to the loop without paying an appropriate amount for the loop costs,<sup>24</sup> the Small ILECS counter that the evidence shows clearly that their affiliates are paying for access to the local loop pursuant to federally tariffed rates and that those payments are being allocated exactly as required under federal

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<sup>21</sup> Small ILECs Opening Brief, 56:21-28.

<sup>22</sup> *Id.*, 60:1-4.

<sup>23</sup> *Id.*, 60:8-11.

<sup>24</sup> *Id.*, 74:12-17.

jurisdictional separations and cost allocation rules.<sup>25</sup> They assert that there is no "free ride" and that the loop is paid for precisely as the Federal Communications Commission (FCC) intends. The Small ILECS claim that TURN and ORA's arguments are inconsistent with these facts and federal rules.<sup>26</sup>

TDS Telecom agrees with the Small ILECs that the Commission cannot and should not "count" broadband revenues or profits towards fulfillment of intrastate revenue requirements.<sup>27</sup>

ORA disputes the Small ILECs arguments. According to ORA, broadband imputation is a ratemaking mechanism well within the Commission's authority to regulate telecommunications companies. It is ORA's contention that no state or federal law prohibits broadband imputation, and the Commission has used similar mechanisms for other utilities.<sup>28</sup> ORA asserts that the Small ILECs cannot have it both ways, that is, they cannot claim that state subsidies for investments in their ISP affiliates' broadband infrastructure are properly due them under regulation, while at the same time arguing that the revenue from those investments is unregulated. ORA argues that if the State of California has the authority to pass SB 379, which allows investments in the "delivery" and "deployment" of broadband-capable facilities to be subsidized by California consumers, despite the FCC's determination that broadband access service is an "information service", then it follows that the State also has the authority to allow

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<sup>25</sup> Small ILECs cite to 47 C.F.R. § 64.901 et seq; 47 C.F.R. § 36.1 et seq; *In the Matter of Appropriate Framework for Broadband Access*, CC Docket No. 02-33, Report and Order, FCC 05-150 ("DSL Deregulation Order").

<sup>26</sup> Small ILECs Opening Brief, 74:12-17.

<sup>27</sup> TDS Telecom Opening Brief, 1:16-17.

the revenues derived from those investments to offset those subsidies.<sup>29</sup> It is ORA's contention that in being subsidized by the A-Fund the Small ILECs have entered into a regulatory pact with California. ORA argues that by advocating for SB 379, the Small ILECs agreed to continue to accept classic rate regulation as a trade-off for receiving state subsidies for broadband investments. ORA asserts that if, as the Small ILECs contend, imputing broadband revenues is forbidden by federal law because it constitutes "common carrier" regulation, then California subsidies for the Small LECs' must also be illegal for the same reason. ORA concludes that neither subsidy nor imputation are illegal because the FCC has not preempted state regulation of rural carriers.<sup>30</sup>

ORA contends that the Small ILECs make unconvincing arguments that broadband imputation would violate Section 275.6. ORA states that the Small ILECs make an unsupported inference from silence in the statute about imputation that affiliate revenues are not permitted to be included in rate design. ORA asserts, despite the Small ILECs claims, there no statute that prevents the Commission from imputing affiliate revenues to a regulated utility's revenue requirement. ORA argues that as the Commission has done in the water context, allocation of non-tariffed revenues can be applied to the revenue requirement.<sup>31</sup>

TURN agrees with ORA and argues that the Commission should not accept the Small ILECs' reasoning regarding imputation and their reading of statutory provisions. TURN contends that the Small LECs would have the Commission

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<sup>28</sup> ORA Reply Brief, 2.

<sup>29</sup> *Id.*

<sup>30</sup> *Id.*, 2, 3.

<sup>31</sup> *Id.*, 10.

ignore the plain language of Section 275.6, with its requirement that the Commission ensure that CHCF-A support is not excessive. TURN states that the Legislature did not tie the Commission's hands on this matter as Small LECs suggest.<sup>32</sup>

ORA disputes the Small ILECs' argument that imputation violates the Takings Clause of the U.S. Constitution. It is ORA's contention that this argument reflects an erroneous understanding of the law, as well as ~~mis~~ mischaracterizes ORA's prior arguments and the relevant law. ORA argues that its imputation proposal involves no taking of non-utility property and should instead be analyzed under the framework of "regulatory takings."<sup>33</sup> ORA asserts that under well-established Constitutional doctrine, "a state scheme of utility regulation does not 'take' property simply because it disallows recovery of capital investments that are not 'used and useful in service to the public'." ORA goes on to argue that under the Fifth Amendment, a ratemaking order only "protects utilities from being restricted to rates that are so 'unjust' as to be confiscatory." ORA states that the Small ILECs have made no showing that its imputation proposal would be confiscatory.<sup>34</sup>

ORA and TURN dispute the Small ILECs public policy contentions that imputation would damage the quality and availability of broadband because it would impair the finances of their ISP affiliates. ORA states that these fears are based on a misapprehension of how broadband imputation would work. ORA asserts that broadband imputation merely "imputes" the ISPs' revenues to the

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<sup>32</sup> TURN Reply Brief, 9.

<sup>33</sup> ORA Reply Brief, 11.

<sup>34</sup> *Id.*, 12-13.

regulated entity, it does not actually “take” any revenues. ORA argues that the ISPs’ rates, terms of service, corporate expenses, and all other aspects of its operations, would remain unaffected. ORA states that imputation would affect only the amount of the regulated entities’ A-Fund subsidy, not the revenues of the ISP and thus not impair the finances of the ISP affiliates in any way.<sup>35</sup>

TURN adds that imputation of broadband revenues would not create incentives to reduce investment in broadband, reduce service quality or curtail retail Internet operations. It is TURN’s contention that under its imputation proposal the Small LECs would continue to have the opportunity to earn a reasonable return on their investment, thus there would be no justification to curtail broadband investment or degrade service quality.<sup>36</sup>

[Several of the parties provided further commentary on broadband revenue imputation, as summarized in the Comments on Proposed Decision section.](#)

#### **2.1.1.2. Discussion**

As indicated supra, in 2012 the California Legislature passed SB 379 which is codified Section 275.6 of the Public Utilities Code. Section 275.6 allows the Small ILECS to include all reasonable investments necessary to provide for the delivery of high-quality communication services and the deployment of broadband-capable facilities in their rate base. As ORA has pointed out, this allows investments in the “delivery” and “deployment” of broadband-capable facilities to be subsidized by California consumers through the CHCF-A program. At its most basic level the argument concerning this issue turns on the question of

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<sup>35</sup> ORA Reply Brief, 31.

<sup>36</sup> TURN Reply Brief, 25.

whether the Small ILECs can claim state subsidies for investments in their broadband capable networks that support broadband and voice, while at the same time arguing that the revenue from affiliates that offer broadband (Internet-access) is unregulated and therefore beyond imputation in the establishment of their revenue requirement and A-Fund subsidy. The Small ILECs, TURN and ORA spent a significant amount of testimony and briefs on this one issue and thus clearly have a keen interest in how it is resolved.

To summarize the parties' positions, the Small ILECs, as well as TDS Telecom, contend that the Commission cannot and should not incorporate broadband revenues or profits into intrastate ratemaking. They assert that doing so would violate state and federal law, harm consumers, upset the incentives for small, rural carriers to deploy broadband, and harm California's universal service and broadband objectives. In contrast, ORA and TURN strongly disagree, arguing that broadband imputation is a ratemaking mechanism well within the Commission's authority to regulate telecommunications companies and that no state or federal law prohibits broadband imputation. Both ORA and TURN also dispute the Small ILECs' public policy contentions that imputation would damage the quality and availability of broadband, because it would impair the finances of the Small ILECs' ISP affiliates.

We do not accept the Small ILECs' contention that the Commission is precluded by federal and state law from imputing broadband revenue when computing the subsidized carrier's draw from the CHCF-A Fund. While Section 275.6 authorized broadband-capable networks to be included in rate base, it is silent on the issue of treatment of broadband-specific revenues for the purpose of calculating the revenue requirement for CHCF-A Fund support. Neither does federal law address the ability of a state to impute broadband-specific revenues

when calculating state universal service fund support for telephone corporations that offer that service through broadband-capable networks. For these reasons, we do not accept that broadband imputation would constitute a violation of the U.S. and California Constitutions as taking of property without just compensation. As stated above, we do not accept the Small ILECs' narrow reading of Section 275.6 and agree with ORA and TURN that the legislature did not intend to limit the Commission's ratemaking authority on this issue.

On the other hand, we do not accept the contentions of ORA and TURN that imposing broadband implementation would have no negative consequences for the Small ILECs and their ISP affiliates through possible service reductions or possible price increases for customers in the rural areas served by Small ILECs. To fulfill the mandate of Section 275.6 to promote investment in broadband-capable networks, we agree with the Small ILECs that their work to build "one network" that is capable of supporting both voice and broadband does not require imputation of broadband revenues since the same network investment would be needed to support high-quality reliable voice service. We are mindful of the importance of the services RLECs provide to the economies of their service territories and the state, and their generally high service quality performance.<sup>37</sup>

We conclude that the circumstances are not yet ripe for the application of broadband revenue imputation. We think it premature to adopt imputation across the board at this time. The broadband ~~imputation provision~~capable network investment provisions of Section 275.6 ~~has~~have been in effect for less

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<sup>37</sup> See Attachment B, *California Wireline Telephone Service Quality, Pursuant to General Order 133 -Calendar Years 2010 through 2013*.



than two years. Not all of the Small ILECs have ISPs that are providing broadband services. Those that are providing broadband directly or through their ISP affiliates are at different stages of broadband deployment in significantly different geographical and demographic situations. Further, the record does not offer standards by which to assess the maturity of broadband deployment in these rural areas. Therefore, it is premature to adopt a standard imputation amidst a nascent regulatory climate and diverse broadband landscape.

In addition, because we have chosen to adopt elsewhere in this decision a comprehensive standard for determining a reasonable level of corporate operations expenses for carriers receiving subsidies from the CHCF-A program, and have decided to increase the basic residential service rate from \$20.25 to ~~\$30.00 the Basic Residential Service Rate, exclusive of other charges, over five years~~ a range of \$30 to \$37, inclusive of additional charges, with specific rates to be set in individual GRCs, the pressures to reduce draws from the CHCF-A program have been addressed separately.

Finally, our preliminary conclusion not to impute broadband revenues at this time is based on the lack of information available on broadband networks in the Small ILEC areas, including information about speed and latency. We await the outcome of the FCC referral to the Federal-State Joint Board on Universal Service, which will provide recommendations on how the FCC should modify the universal service contribution methodology.<sup>38</sup> Further, the Broadband Networks and Universal Service studies that will be completed in Phase 2 of this proceeding

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<sup>38</sup> Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Universal Service Contribution Methodology, WC Docket No. 06-122, A National Broadband Plan for Our Future, GN Docket No. 09-51.

will evaluate broadband build-out, including speed levels. The results of the studies will help the Commission better evaluate investment needs, along with information that accumulates through GRCs as § 275.6 catalyzes broadband build-out.

~~We therefore~~Therefore, although the Commission has authority to impute, broadband revenues, we will not impose broadband imputation at this time, continuing at least through the first rate case cycle for each Small ILEC following this decision. We plan to revisit the issue in ~~five years~~Phase 2 when the relationship between broadband service and the provision of voice services is clearer for each of these companies, and after review of the Broadband Network and Universal Service studies to be conducted in Phase 2. In Phase 2 we will determine whether broadband revenue should be imputed in subsequent GRC cycles.

**2.1.2. ~~B.~~ Can and should the Commission standardize costs in considering the Small ILEC's revenue requirement**

Related to the overall costs to the CHCF-A program is the question of whether the Commission should have a standard methodology to determine a reasonable level of expenses/costs for activities in which the companies that draw from the CHCF-A engage. Specifically, should the Commission adopt a standard for determining a reasonable level of corporate expenses?

**2.1.2.1. Comments on the Rulemaking**

ORA argues that we should adopt the FCC standards for corporate expense limits. ORA points to Assembly Bill (AB) 1693, which would have limited the timeframe for the Commission to complete the GRCs for each of the Small ILECs.

ORA states that even though the Governor vetoed AB 1693, his veto message encouraged the Commission to create a GRC Plan to spur timely completion of the Small ILECs' GRCs. ORA supports this goal. In order to timely complete the GRCs, ORA argues that it is critical that the Commission adopt the FCC corporate expenses limits as a standard for what is a reasonable level of corporate operations.<sup>3839</sup> ORA contends that California has not adopted any "bright line" standards for what constitutes a reasonable level of corporate operations expenses and instead considers these expenses on a case by case basis in the GRC process. ORA argues that adopting the FCC standards would reduce the amount of litigation over these costs.<sup>3940</sup>

The Small ILECs acknowledge that it is entirely appropriate that the Commission review corporate operations expenses in the course of their GRCs but that the Commission should not adopt the FCC's corporate expense caps as strict limits for intrastate revenue requirements. The Small ILECs acknowledge that ORA's proposal to adopt interstate caps could be used to calculate recoverable intrastate expenses, but contend this would be a crude substitute for the individualized company-specific review appropriate for a GRC.<sup>4041</sup> The Small ILECs argue that: 1) The FCC's corporate caps are not designed to be measurements of the corporate expense component of intrastate revenue requirement, so their importation into the California ratemaking process would be a non sequitur; 2) The corporate caps are poor proxies for the analysis of

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<sup>3839</sup> ORA Opening Brief, 6, § IV.

<sup>3940</sup> ORA Opening Brief, 7.

<sup>4041</sup> Small ILEC Opening Brief, 94, § V.

expenses that takes place in a rate case;<sup>4142</sup> 3) The caps are unlikely to produce reliable conclusions regarding the reasonableness of corporate expenses for California companies; 4) The FCC caps themselves have significant methodological flaws that California should not replicate by endorsing their use in intrastate ratemaking;<sup>4243</sup> and 5) The problems presented by use of the FCC caps would be compounded if they were applied outside of the rate case process.<sup>4344</sup>

In response to the Small ILECs contentions ORA states that: 1) Inasmuch as the FCC does not set any revenue requirements, the Small ILECs' contention is true. However, ORA notes that the FCC's purpose is to limit the amount of a Small ILEC's corporate operations expenses that are eligible for federal subsidies. The FCC's intent in adopting these standards was to limit the recovery of corporate operations expense, while also updating the formula for limiting their eligibility since the formula's last update in 2001. ORA contends that the FCC adopted these standards for exactly the same reason articulated by the Commission in this OIR, to limit corporate expenses that are eligible for state subsidies;<sup>4445</sup> 2) ORA contends that the Small LECs do not acknowledge the inconsistency in their position, that doing analysis in each individual case by definition will increase the amount of investigation, data gathering, analysis, and litigation that will be required to determine the allowable corporate expense

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<sup>4142</sup> *Id.*, 95:17-18.

<sup>4243</sup> *Id.*, 96:21-22.

<sup>4344</sup> Small ILEC Opening Brief, 97:5-6.

<sup>4445</sup> ORA Reply Brief, 41.

levels;<sup>4546</sup> 3) ORA asserts that the Small LECs provide no cost studies or data to show that doing business in California's rural areas is any different than rural areas in other states. ORA contends that Small ILECs make unsupported allegations that California's rural areas have higher corporate expense costs than elsewhere and that there is no basis upon which to conclude that the FCC needed to make state-specific findings for its corporate expenses standards to be reasonable;<sup>4647</sup> 4) ORA argues that the Small ILEC's claims that the FCC's corporate expense standards contain "flaws" such as the failure to consider "terrain, customer density, and the specific regulatory and consumer issues" for each Small ILEC underscores the advisability of streamlining and simplifying the calculation of corporate standards.<sup>4748</sup> ORA asserts that if the Commission were to consider corporate standards with such granular specificity in each GRC, it could never meet Governor Brown's mandate that the CPUC create a GRC Plan to encourage timely completion of the Small LECs' GRCs;<sup>4849</sup> and 5) ORA contends it has not made any recommendation in this proceeding (in its testimony, briefs or cross-examination) to transform the annual filing process into a vehicle to reduce corporate expenses and that it is therefore outside the scope of ORA's arguments.<sup>4950</sup>

In their reply brief the Small ILECs reiterated the stance from their opening brief that the use of federal corporate expense caps in intrastate ratemaking

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<sup>4546</sup> *Id.*, 42.

<sup>4647</sup> ORA Reply Brief, 42.

<sup>4748</sup> *Id.*, 43.

<sup>4849</sup> *Id.*

<sup>4950</sup> *Id.*

presents several insurmountable problems. The Small ILECs argue that since these caps are designed to limit federal contributions to corporate operations without regard to intrastate revenue requirement, and since they do not account for company-specific circumstances or California-specific cost drivers, they represent only a crude tool for estimating the proper level of corporate operations expense for any particular company. It is the Small ILEC's contention that to the extent that ORA's rote application in a rate case or another rate proceeding would be "efficient," it would be a shortcut to an inaccurate result.<sup>5051</sup>

TDS Telecom recommends that the Commission permit but not require small LECs to employ corporate expense levels adopted by the FCC in their rate cases. TDS Telecom states that this option should be made available to Small ILECs with expenses below the FCC levels and to those Small ILECs whose expenses are above the FCC levels but which are willing to accept the FCC levels to avoid the expense and uncertainty of rate cases. TDS Telecom argues that the GRC and means test filings of these small LECs would be streamlined because their corporate expense levels would be accepted as reasonable unconditionally by the Commission and its staff without the need for litigation.<sup>5152</sup>

#### **2.1.2.2. Discussion**

A primary goal of the instant OIR is for the Commission to determine how the CHCF-A program can more efficiently and effectively meet its stated goals of providing affordable, widely available, safe, reliable and high quality communications services for rural areas of the state. Adopting a uniform

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<sup>5051</sup> Small ILECs Reply Brief, 47:17-25.

<sup>5152</sup> TDS Telecom Reply Brief, 1:18-28.

standard for determining a reasonable level of corporate operations expenses for carriers receiving subsidies from the CHCF-A program allows the program to achieve its goals while ensuring that the level of support is not excessive or wildly disparate across companies, and avoids imposing an undue burden on California ratepayers who contribute to the fund. We believe that the FCC's Corporate Expense Caps are a rationale mechanism for calculating and determining a reasonable level of corporate expenses for those carriers drawing from the Fund. Adopting and applying the FCC Corporate Expense Caps will cap the amount of corporate expenditures that can be recovered from the CHCF-A program, and create incentives to align expenditures with the cap to reduce rate case litigation costs. Additionally, applying a rebuttable presumption to the corporate cap model, as shown below, offers the Commission and parties the flexibility necessary to account for unique situations.

~~If a carrier's actual corporate expense amounts exceed the caps, that carrier can file a request for additional support from the CHCF-A program in their GRC application. The carrier must demonstrate (with documentation and calculations) why additional support, above the cap, is reasonable and necessary. Such requests will be reviewed on a case-by-case basis taking into account any and all unique circumstances effecting the carrier's corporate cost and documented expenditures.~~

The corporate cap will be applied as a rebuttable presumption in the context of establishing revenue requirement in the GRCs.<sup>53</sup> The rebuttable presumption will be available in either direction whether expenditures fall above

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<sup>53</sup> See Comments on Proposed Decision regarding for comments on the rebuttable presumption.

or below the cap. If expenditures exceed the cap, there would be a presumption of unreasonableness and carriers would have the opportunity to rebut the presumed level of expenses imposed under the cap by demonstrating that a different level of corporate expenses is reasonable. Expenses that fall below the cap would be presumed reasonable subject to an opportunity by other parties to rebut that conclusion in the GRC. The Commission declines to prescribe the type of factors to rebut a presumption, as such factors may be developed in the GRCs.

As noted by ORA, *supra*, in his veto message for AB 1693 the Governor encouraged the Commission to create a GRC Plan to spur timely completion of the Small ILECs' GRCs. In conformance with the Governor's veto message the Assigned Commissioner will issue a Ruling soliciting comments in order to create a GRC Plan for the Small ILECs which will be implemented in an interim decision between Phase 1 and 2 of the instant proceeding.

### **2.1.3. Waterfall Adjustment Issues**

We will seek additional comments on this set of issues and address adjustment to the Waterfall mechanism through an Assigned Commissioner's Ruling (ACR) and interim PD between Phase 1 and Phase 2 of the instant proceeding.

### **2.2. Should the Small ILEC Territory be Opened to Wireline Competition?**

The instant OIR seeks input into the question of whether the Commission can and should open the Small ILEC's territories to wireline competition in the same way that the territories of the large and mid-sized LEC territories have been opened.



**2.2.1. Comments on the Rulemaking**

The CCTA asserts that the Commission must open the Small ILEC territory to competition in order to avoid interference with federal law, state law and the Commission's own prior Decisions. CCTA argues that opening these rural areas is not only required by law, but doing so advances infrastructure deployment by competitors that do not and cannot rely on high cost subsidies, promotes broadband adoption, and promises to offer many rural consumers voice and other broadband services already offered to their urban counterparts.<sup>5254</sup> This view is strongly supported by the California Association of Competitive Telecommunications Companies (CALTEL) and Big River Telephone Company (BRT).

CALTEL cites Sections 251(a) and 251(b) of the Federal Telecommunications Act of 1996 (96 Act), codified in the Communications Act of 1934,<sup>5355</sup> mandating that each telecommunications carrier interconnect directly or indirectly with the facilities and equipment of other telecommunications carriers, and comply with certain standards such as resale, number portability, dialing parity, access to rights-of-way, and reciprocal compensation, federal law mandates that the territories of RLECs be opened to competition.<sup>5456</sup> CALTEL rebuts the Small ILEC's characterization of Sections 251(a) and (b) of the 96 Act as dealing solely with interconnection, the duty of each telecommunications carrier to carry and complete other carriers' calls, and having nothing to do with

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<sup>5254</sup> CCTA Opening Brief, 1.

<sup>5355</sup> 47 U.S.C. §§ 251(a) and (b).

<sup>5456</sup> CALTEL Opening Brief, 2.

mandatory interconnection under Section 251 (c) to foster local competition. CALTEL argues that the plain language of the statute, and application of it through consistent FCC decisions recognizes that its purpose, including Section 251 as a whole, was to open local telecommunications markets to competition.<sup>5557</sup> CCTA agrees with CALTEL and contends that Section 251 obligates, among other things, all telecommunications carriers to interconnect directly or indirectly with the facilities and equipment of other telecommunications carriers. CCTA asserts that Section 251(b) of the 96 Act obligates all local exchange carriers to not prohibit resale of telecommunications services, to provide number portability and dialing parity, to afford access to rights of way, and to establish reciprocal compensation arrangements for the transport and termination of telecommunications.<sup>5658</sup>

Under 47 U.S.C. Section ~~254~~251(c), ILECs must negotiate in good faith interconnection agreements for the transmission and routing of telephone exchange service and exchange access and permit a requesting telecommunications carrier to interconnect to any technically feasible point in the network. 47 U.S.C. Section ~~254~~251(f)(1)(a) exempts rural telephone companies from the ~~Interconnection~~interconnection requirements of 47 U.S.C. Section ~~254~~251(c) “until (i) such company has received a bona fide request for interconnection, services, or network elements, and (ii) the State commission determines (under subparagraph (B)) that such request is not unduly

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<sup>5557</sup> *Id.*, 3.

<sup>5658</sup> CCTA Opening Brief, 2.

economically burdensome, is technically feasible, and is consistent with section 254 of this title (other than subsections (b)(7) and (c)(1)(D) thereof)."

The process for review of an interconnection request with a rural telephone company is laid out in 47 U.S.C. Section ~~254~~251(f)(1)(b):

A "party making a bona fide request of a rural telephone company for interconnection, services, or network elements shall submit a notice of its request to the State commission. The State commission shall conduct an inquiry for the purpose of determining whether to terminate the exemption under subparagraph (A). Within 120 days after the State commission receives notice of the request, the State commission shall terminate the exemption if the request is not unduly economically burdensome, is technically feasible, and is consistent with section 254 of this title (other than subsections (b)(7) and (c)(1)(D) thereof). Upon termination of the exemption, a State commission shall establish an implementation schedule for compliance with the request that is consistent in time and manner with Commission regulations."

No bona fide request for interconnection is at issue in this proceeding. Instead, this proceeding seeks to determine whether as a matter of federal or state law, and CPUC analysis of the best policy, areas served by RLECs should be open to competition from wireline telecommunications carriers.

CCTA argues that the Small ILECs have claimed that the rural exemptions under Section 251 (f)(1) indicate that the obligations under Section 251(a) and 251(b) do not apply to RLECs. CCTA contends that any potential ambiguity in these provisions was removed more than three years ago when the FCC clarified the applicability of these statutes to the obligations of RLECs. CCTA cites the FCC's 2011 Rural Declaratory Ruling, ~~57~~59 in which it asserts the FCC clarified that LECs are obligated to fulfill *all* of the duties set forth in Sections 251(a) and (b) of

the Act, including the duty to interconnect and exchange traffic, even if the LEC has a rural exemption pursuant to Section 251(f)(1) of the 1996 Act.<sup>5860</sup>

In its May 2011 Rural Declaratory Ruling, the FCC concluded that “a uniform, national policy concerning the scope of the rural exemption is necessary to promote local competition, prevent conflicting interpretations of carriers' statutory obligations under the Act, and eliminate a potential barrier to broadband investment.”<sup>5961</sup> The FCC determined:

Consistent with Commission precedent, we reaffirm that all telecommunications carriers, including rural carriers covered by section 251(f)(1), have a basic duty to interconnect their networks under section 251(a) and that all LECs, including rural LECs covered by section 251(f)(1), have the obligation to comply with the requirements set forth in section 251(b). We also clarify that a rural carrier's exemption under section 251(f)(1) offers an exemption only from the requirements of section 251(c) and does not impact its obligations under sections 251(a) or (b).<sup>6062</sup>

Under this FCC Decision, ~~RLECs are~~ RLECs are exempt from the Section 251(c) requirement that “Incumbent Local Exchange Carriers must negotiate interconnection agreements in good faith and permit a requesting telecommunications carrier to interconnect to any technically feasible point in the network.” Like other telecommunications carriers, rural carriers have duties

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<sup>5759</sup> CALTEL Opening Brief, 4.

<sup>5860</sup> *Id.*, t 3.

<sup>5961</sup> *In the Matter of Petition of Crc Commc'ns of Maine, Inc. & Time Warner Cable Inc. for Preemption Pursuant to Section 253 of the Commc'ns Act, As Amended A Nat'l Broadband Plan for Our Future Developing A Unified Inter-carrier Comp. Regime*, 26 F.C.C. Rcd. 8259, 8267 (2011) [hereinafter *Rural Declaratory Ruling*].

<sup>6062</sup> *Id.*

under Section 251(a) and (b) to interconnect with other carriers for the purpose of carrying and completing calls and exchanging traffic, and must comply with certain standards such as resale, number portability, dialing parity, access to rights-of-way, and reciprocal compensation. The FCC's 2011 Rural Declaratory Ruling distinguishes between ~~mandatory~~<sup>the</sup> interconnection requirement for local competition under Section 251(c), from which RLECs are exempt, and the exchange of traffic required of the RLECs and other telecommunications carriers under Section 251(a) and (b).

CALTEL argues that the FCC followed up on the RLEC Declaratory Ruling in a subsequent case by preempting a state commission which did not comply with the requirements of federal law under Section 251.<sup>6163</sup> CALTEL states that the FCC pointed out that "one of the principal objectives of the 1996 Act is opening local exchange and exchange access markets to competition."<sup>6264</sup>

On the state level,<sup>63</sup> BRT argues that both the Commission and the California Legislature have determined that competition in the Small ILEC territories will benefit Californians. BRT cites our decision in D.95-07-054, asserting that the Commission intended "to permit the opening of all telecommunications markets, including small and mid-sized LECs, to competition" and to establish necessary rules for market entry by January 1, 1997.<sup>6365</sup> BRT argues that in D.97-09-115, the Commission reiterated that it would develop rules for local exchange competition

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<sup>6163</sup> CALTEL, Opening Brief~~at~~<sup>4</sup> 4.

<sup>6264</sup> *Id.* (citing *In the Matter of Time Warner Cable Inc. Pursuant to Section 252(e)(5) of the Communications Act for Preemption of the Jurisdiction of the North Carolina Rural Electrification Authority Regarding Arbitration of an Interconnection Agreement with Star Telephone Membership Corporation*, Memorandum and Order, DA 13-2117, WC Docket No. 13-204 (2013).

<sup>6365</sup> BRT Opening Brief, 1.

in the small ILEC's territories after opening large and mid-size ILECs' territories to competition.<sup>6466</sup> BRT observes that to date, the Commission has not set forth the rules for competitive entry into the Small ILECs' territories, but argues that there has been no change in the Commission's policy or intent.<sup>6567</sup> CCTA agrees that state law is consistent with federal law in this regard but even if it were not, CCTA claims that the FCC's Rural Declaratory Ruling make clear that under federal law, the Commission must open the Small ILEC territories to competition.<sup>6668</sup>

The Small ILECs state that the Commission has jurisdiction over market entry for public utilities, which includes authority to determine when and to what extent a market should be opened to competition.<sup>69</sup> They also assert that Sections 251(a) and (b) do not address the issue of competition. They assert that Section 251(a) establishes a general duty of telecommunications carriers to interconnect and that many carriers interconnect without competing in the same local markets.<sup>70</sup> They point out that a carrier's obligation and duty to interconnect does not in and of itself constitute a directive to state commissions to open local markets to competition.<sup>71</sup>

The Small ILECs argue that opening their service areas to wireline CLEC competition would be contrary to the public interest because it will strand

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<sup>6466</sup> *Id.*

<sup>6567</sup> *Id.*

<sup>6668</sup> CCTA Opening Brief, 4.

<sup>69</sup> Small ILECs Reply Brief, 49-50.

<sup>70</sup> Small ILECs Reply Brief, 51.

<sup>71</sup> Small ILECs Reply Brief, 54.

existing investments made by Small ILECs without any countervailing benefits for consumers. The Small ILECs argue that because they are COLRs (Carriers of Last Resort), they are obligated to serve all the customers in their service area who request service, unless a request for service is prohibitively expensive or otherwise ~~unreasonable~~The unreasonable. The Small ILECs assert that as a result of their COLR obligations, they are required to maintain robust networks that are capable of providing reliable services for all current and future customers.<sup>6772</sup>

The Small ILECs further argue that CLECs are generally not COLRs and are under no obligation to serve. The Small ILECs assert that the CLEC business model is generally based on having sufficient subscribers to cover the costs of infrastructure investments and that ~~his~~this business model means that CLECs must typically focus on businesses customers or target more densely-populated towns that produce higher revenues at lower costs.<sup>6873</sup> The Small ILECs ~~observes~~observe that CALTEL has expressed only a regulatory policy interest in opening the rural service areas to competition, not a demonstrable service interest, and asserts that CALTEL has acknowledged that its member CLECs have traditionally focused on business customers.<sup>6974</sup> An analysis of existing Voice ~~Over~~over Internet Protocol (VoIP) and wireless competitors in the rural service areas confirms that competitors tend to serve only small portions of any of the Small ILECs' service areas, and CLECs are likely to "cherry pick" customers rather than serve significant portions of rural service territories. The Small ILECs claim

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<sup>6772</sup> Small ILECs Opening Brief, 99:4-14.

<sup>6873</sup> *Id.*, 99:16-22.

<sup>6974</sup> *Id.*, 99:22-25.

that these small portions are generally the higher-density, lower-cost, and higher-revenue areas of a company's service territory.<sup>7075</sup>

The Small ILECs also argue that if CLEC competition is allowed in their service areas it will ~~only~~ undermine universal service principles by increasing the Small ILECs' costs in fulfilling their COLR obligations because it is improbable that CLEC competitors will be capable of reaching new or additional customers with reliable service.<sup>7176</sup> The Small ILECs state that if CLECs are permitted to operate in their service territories and are able to compete successfully, CLEC success must be measured against the likely increased burden on the CHCF-A fund. The Small ILECs claim that their COLR obligations require them to maintain robust and reliable networks for current and potential future customers and that most of the costs of providing this service are fixed and will not fluctuate despite increases or decreases in their customer bases.<sup>7277</sup> The Small ILECs assert that if those costs are spread among fewer customers, the cost per customer will generally increase. The Small ILECs further argue that if the customer base declines, so will end-user revenue. They point out that end-user revenue is one source of cost recovery designed to meet their revenue requirement. The Small ILECs state that the CHCF-A program is targeted to fulfill their revenue requirements after consideration of all other sources of cost recovery; any decreases in end-user revenues will generally result in a corresponding increase in a carrier's draw from the CHCF-A Fund.<sup>7378</sup>

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<sup>7075</sup> Small ILECs Opening Brief, 99:26 & 100:1-5.

<sup>7176</sup> *Id.*, 101:26-28 & 102:1-2.

<sup>7277</sup> *Id.*, 102:7-14.

<sup>7378</sup> Small ILECs Opening Brief, 102:15-20.



TDS Telecom concurs with the Small ILEC recommendation that the territories they serve should not be opened to wireline competition. TDS Telecom agrees with the Small ILECS that neither state nor federal law requires that the Commission open small LEC territories to competition.<sup>7479</sup> TDS Telecom states that it is open to the authorization of wireline competition in the territories of those Small ILECs which elect not to be subject to rate-of return regulation. This would be done under TDS Telecom's proposed Small Uniform Regulatory Framework plan or other any other plan that permits small LECs to opt out of rate-of-return regulation.<sup>7580</sup>

### **2.2.2. Discussion**

We acknowledge that competition is an important goal in the territories covered by the CHCF-A program, but we must balance that objective with other goals such as federal and state universal service in 47 U.S.C. Section ~~254~~254 and Public Utilities Code Section 871, and the ~~universal service~~, public safety, reliability, affordability, and economic development goals of California state law. Although CALTEL, CCTA and BRT have all argued that it is appropriate and necessary to open the Small ILECs' service territory to wireline competition, we preliminarily conclude that this result is not dictated by either federal or state law. ~~Federal law does not mandate that RLECs negotiate interconnection agreements to facilitate local competition and the FCC has specifically recognized the RLECs' statutory exemption from this requirement. Neither State law nor prior Commission decisions mandate that the areas served by RLECS be opened to~~

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<sup>7479</sup> TDS Telecom Opening Brief, 2:5-12.

<sup>7580</sup> *Id.*

~~wireline competition~~, and is not supported by the evidentiary record in this proceeding.

We note that all CPCNs issued to CLECs since the passage of the '96 Act have not included authority to offer service in the territories of the Small ILECs. Notwithstanding that fact, so far as we are aware, also since passage of the '96 Act, no service provider has made a bona fide request to a Small ILEC (also known as a Rural Local Exchange Carrier (RLEC) seeking access to elements set forth in Section 251(c) of the Act. Indeed, parties at the All-Party Meeting on December 11, 2014 agreed that competitors are not asserting they have been denied competitive entry based on an inability to access elements set forth in Section 251(c) (duty to negotiate, interconnection, unbundled access, duty to offer services at resale rates, and collocation).<sup>81</sup> Accordingly, no request for interconnection under Section 251(c) in Small ILEC territories is presented or ripe for review.

Similarly, so far as we are aware, no competitor has sought access to elements set forth in Section 251(b) (resale, number portability, dialing parity, access to rights-of-way and reciprocal compensation) since passage of the '96 Act. Also at the All-Party Meeting, there was agreement that competitors engage in traffic exchange and calls are completed under Section 251(a) (general duty to interconnect). Compliance with the requirements of Section 251(a) is not at issue in this proceeding and no complaint about duty to interconnect for the purpose of traffic exchange with Small ILECs is at issue in this proceeding.

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<sup>81</sup> Interconnection under Section 251 (c) is currently available in areas of California served by carriers other than small ILECs upon a bona fide request of a CLEC that has a CPCN.

Traffic exchange interconnection under Section 251(a) differs from “interconnection” for “local competition” under Section 251(c) in that the former allows callers from one telephone company to communicate with customers of another telephone company, but does not allow access to “unbundled network elements” under Section 251(c) that would allow a CLEC to offer local exchange service within the service territory of a carrier to whom competitive interconnection is allowed. While both interconnection and competition play an important role in telecommunications markets, their purposes are separate and distinct. The purpose of wireline local competition is to allow other wireline carriers to offer competing telecommunications services to end-users. The purpose of rules requiring interconnection, on the other hand, is to allow carriers to link their networks and equipment to facilitate mutual exchange of traffic. The FCC rule, 47 C.F.R. Section 51.5 defines interconnection as “the linking of two or more networks for the mutual exchange of traffic.”

The FCC, in its 2011 Declaratory Ruling, clarified that the rural exemption from Section 251(c) requirements does not remove Sections 251(a) and (b) obligations. We do not change or interfere with Section 251 obligations. If a CLEC wants to access Section 251(b) or (c) elements, the CLEC should follow the procedures outlined in Section 251, including making a bona fide request to the Commission and state whether it has made a good faith effort to negotiate access to those elements with the Small ILECs.

Finally, we are not aware of any request from any RLEC for a rural exemption under Section 251(f) of the Act. We note that any future interconnection request under Section 251(c) may be affected by any filing submitted under Section 251(f) to request this Commission to apply the federal statutory rural exemption to areas served by Small ILECs.

During the December 11, 2014 All-Party Meeting, CALTEL expressed interest in access to the five elements in Section 251 (b) to facilitate “simple resale” and enable local competition. Section 251(b) requires local exchange carriers to make available the following five elements:

- 1) Resale of its telecommunications services;
- 2) Number portability;
- 3) Dialing parity (the duty to provide dialing parity to competing providers of telephone exchange service and telephone toll service, and the duty to permit all such providers to have nondiscriminatory access to telephone numbers, operator services, directory assistance, and directory listing, with no unreasonable dialing delays);
- 4) Access to poles, ducts, conduits, and rights of way; and
- 5) Duty to establish reciprocal compensation arrangements for the transport and termination of telecommunications.<sup>82</sup>

Also at the December 11, 2014 All-Party Meeting, CALTEL and CCTA acknowledged that they have filed no bona fide request for access to the elements described in Section 251(b). They attributed the absence of any such request due to the limitations in the CPCNs the Commission issued that do not authorize CLECs to offer service in areas served by Small ILECs. No petition has been received by this Commission to change the CPCN service areas to allow for service in areas served by Small ILECs. Any such petition to provide service in rural markets may be affected by other petitions that may be filed to invoke the rural exemption under the '96 Act that would require this Commission to determine whether such competition or interconnection is in the public interest or

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<sup>82</sup> 47 U.S.C. Section 251(b).

would impose an adverse economic impact on telecommunications users, among other factors.

Federal law provides a process whereby Small ILECs can petition a state Commission for the exemption from the requirements of Sections 251(b) and (c). Under Section 251(f)(2) “a local exchange carrier with fewer than 2 percent of the Nation’s subscriber lines installed in the aggregate nationwide may petition a State commission for a suspension or modification of the application of a requirement or requirements of subsection (b) or (c) of this section to telephone exchange service facilities specified in such petition.” The ’96 Act provides the standards by which the state Commission must evaluate and shall grant such a petition as follows:

The State commission shall grant such petition to the extent that, and for such duration as, the State commission determines that such suspension or modification – (A) is necessary – (i) to avoid a significant adverse economic impact on users of telecommunications services generally; (ii) to avoid imposing a requirement that is unduly economically burdensome; or (iii) to avoid imposing a requirement that is technically infeasible; and (B) is consistent with the public interest, convenience, and necessity.”<sup>83</sup>

The statute provides the timeframe for action upon receipt of such a petition: “The State commission shall act upon any petition filed under this paragraph within 180 days after receiving such petition. Pending such action, the State commission may suspend enforcement of the requirement or requirements to which the petition applies with respect to the petitioning carrier or carriers.”<sup>84</sup>

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<sup>83</sup> 47 U.S.C. Section 251(f)(2).

<sup>84</sup> Id.

We also know that, since the passage of the '96 Act, the Small ILECs have not filed with this Commission a request under Section 251(f) for the suspension or modification of the requirements under Sections 251(b) and (c). Throughout this proceeding, the Small ILECs have often cited in their briefs, comments, in the hearings and at the All-Party meeting, the "rural exemption" under Section 251(f), but they have not filed a petition for exemption, suspension, or modification of the application of interconnection obligations under Section 251(c) or the elements of Section 251(b).

Neither have the Small ILECs filed a petition that would require evaluation of a rural market exemption under Section 253(f). Section 253(a) states that "No State or local statute or regulation, or other State or local legal requirement, may prohibit or have the effect of prohibiting the ability of any entity to provide any interstate or intrastate telecommunications service."<sup>85</sup> Section 253(f) recognizes that a state Commission may consider a petition for a rural market exemption:

It shall not be a violation of this section for a State to require a telecommunications carrier that seeks to provide telephone exchange service or exchange access in a service area served by a rural telephone company to meet the requirements in section 214(e)(1) of this title for designation as an eligible telecommunications carrier for that area before being permitted to provide such service. This subsection shall not apply – (1) to a service area served by a rural telephone company that has obtained an exemption, suspension, or modification of section 251(c)(4) of this title that effectively prevents a competitor from meeting the requirements of section 214(e)(1) of this title; and (2) to a provider of commercial mobile services."<sup>86</sup>

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<sup>85</sup> 47 U.S.C. Section 253.

<sup>86</sup> 47 U.S.C. Section 253(f).

47 U.S.C. Section 214(e)(1) establishes the standards and process by which a state may designate a common carrier as an eligible telecommunications carrier (ETC), eligible for universal service funding. A distinct standard for applications for ETC status in a rural market is set by Section 214(e)(2): "Before designating an additional eligible telecommunications carrier for an area served by a rural telephone company, the State commission shall find that the designation is in the public interest." No application for ETC status in a rural market served by Small ILECs has been received by any CLEC proposing to offer wireline service in competition with Small ILECs.

Section 253(b) also allows the states to adopt measures that are necessary to advance the public interest objectives such as universal service, public safety and welfare and continued quality of telecommunications services. Section 253(c) provides state and local governments with authority to manage public rights-of-way used by telecommunications carriers to provide their services. Section 253 is intended to foster cooperation between the FCC and the state and local governments in promoting competition.

CCTA argued at the All Party meeting on December 11, 2014 and stated in its written comments that Section 253(a) requires this Commission to open the rural markets served by Small ILECs to competition. Their argument, however, did not recognize the statutory process in Section 253(f) which allows the Commission to evaluate whether any request for interstate or intrastate telecommunications service offerings in a local market serves the public interest. Neither does this argument or that of CALTEL recognize the process and standards under Section 251(f) that requires, upon a petition for exemption, modification, or suspension of the obligations of Section 251(b) and/or (c), that the Commission shall grant such a petition if it "is necessary – (i) to avoid a

significant adverse economic impact on users of telecommunications services generally; (ii) to avoid imposing a requirement that is unduly economically burdensome; or (iii) to avoid imposing a requirement that is technically infeasible; and (B) is consistent with the public interest, convenience, and necessity.”

Based on our findings about the rural territories the RLECs serve, and specifically, customer concerns about the potential for service degradation in a competitive market that would primarily favor larger business customers, and based on the procedural status regarding lack of requests for interconnection and exemption under federal law, we make a preliminary finding that it is not in the public interest to open the Small ILECs territories to wireline competition at this time.

As described in more detail below, in Phase 2 of this decision we will conduct Broadband Networks and Universal Service studies to analyze the potential impact of competition in each Small ILEC territories on universal service, reliability, safety, just and reasonable rates, deployment of broadband capable networks, deployment and maintenance of high-quality voice networks, on the economic impact on users of telecommunications services, and on the High Cost A Fund. Review of these studies in the Phase 2 decision will provide the facts necessary to evaluate the effect of potential CLEC competition in specific areas served by Small ILECs. The studies will also inform the GRCs that will begin after the adoption of the Phase I decision to help determine what investments are needed to deploy broadband capable and high-quality voice networks in accordance with Public Utilities Section 275.6.

The CPUC will defer consideration of any request filed and received subsequent to this Phase I decision to amend CPCNs to include Small ILEC areas or for access to Section 251(b) elements or interconnection under Section 251 (c).



or for a petition under Section 251(f)(2) to suspend or modify the application of the requirements of Section 251(b) or (c), or a petition under Section 253 (f) until the Broadband Networks and Universal Service study is completed in Phase 2 of this proceeding for that Small ILEC area and the Commission has evaluated the study to determine whether or not that area should be opened to CLEC competition. That determination will be based on the facts and assessment of that area, weighing universal service, public safety, reliability, consumer protection, and High Cost A Fund costs and impacts, the effect on federal funding, efficiency, and the benefits or consequences of competition, and the standards and requirements of federal and state law. The Broadband Networks and Universal Service studies are consistent with our “ground-truthing” effort through the CPUC’s Broadband Mapping program that supports our analysis of where broadband investments may be merited through the California Advanced Services Fund. Such studies will allow for evidence-based decision-making based on local conditions.

This location-specific fact-finding is merited in light of the variations between the areas served by California’s 13 Small ILECs, that differ in terrain from mountainous to desert, have varying levels of population and visitors, differ in service costs, and have different levels of barriers to service including lack of access to electricity in parts of some service territories such as portions of Siskiyou telephone. Access to electricity affects telecommunications access because of power needed for high-quality telephone service and for broadband service via fiber. Larry Thompson testified at the evidentiary hearings in this proceeding that “fiber can go out over 12 miles without electronics...You have electronics in central office and a little piece on the side of the home. Now, if you’re more than 12 miles, then you would have to put an electronic thing out there to essentially

boost the signal to get all the way out to the customer.”<sup>87</sup> Mr. Thompson also testified that access to commercial power affects costs and ability to deploy fiber.<sup>88</sup>

Commission review of any such relevant petitions which may be filed subsequent to this Phase I Decision must follow the area and fact specific Broadband Networks and Universal Service studies we will conduct in Phase 2 of this proceeding. At this time, a final decision on whether to open some or all of the Small ILEC areas to competition or final disposition of any petitions for a rural exemption, to amend the service area of CPCNs to include Small ILEC-served areas, or for access to Section 251(b) elements, to interconnection under Section 251(c), to provide facilities-based service in small ILEC areas with or without Section 251(b) elements or interconnection under Section 251(c), or to allow interstate and interstate telecommunications service in Small ILEC markets under Section 253 is not ripe for review.

As to state law, there is no mandate under the Public Utilities Code that requires the Commission to facilitate competition in local Small ILEC markets. Public Utilities Code Section 709.5(a)<sup>89</sup> states that “It is the intent of the Legislature that all telecommunications markets subject to commission jurisdiction be opened to competition not later than January 1, 1997.” This is a statement of legislative intent, which does not carry the force of law. Public

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<sup>87</sup> Evidentiary Hearing, 11-11-007, Sept. 4, 2014, at 756-757, Testimony of Larry Thompson.

<sup>88</sup> Id.

<sup>89</sup> Pub. Util. Code § 709.5(a) states “It is the intent of the Legislature that all telecommunications markets subject to commission jurisdiction be opened to competition not later than January 1, 1997. The commission shall take steps to ensure that competition in the telecommunications markets is fair and that the state’s universal service policy is observed.”

Utilities Code Section 275.6<sup>90</sup>, which provides the Commission with broad authority to establish and administer the A-Fund, similarly does not impose a mandate on the Commission to open Small ILEC territories to wireline competition.

~~The~~Also, the decision CALTEL cites, for ~~arguing~~the proposition that the RLEC territories should be opened to competition, D.95-07-054, neither binds this Commission's action, nor provides guidance for the Commission's evaluation of whether opening the areas served by RLECs is appropriate at this time. In 1995 through D.95-07-054, the Commission opened to competition the areas served by the larger ILECs, Pacific Bell, now known as AT&T, and GTE, now known as Verizon.<sup>91</sup> D.95-07-054 analyzed whether areas served by non-rate-regulated ILECs should be open to competition, and did not consider whether areas served by RLECs should be open to competition.

Presaging the debate that continues nearly twenty years later about the impact of local competition on service in Small ILEC areas, in D.95-07-054 the Small ILECs argued that hearings would be needed before imposing the rules adopted for competition in Pacific Bell and GTE territories to the Small ILEC areas.<sup>92</sup> The Small ILECs argued in D.95-07-05 that the effect of any such

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<sup>90</sup> Pub. Util. Code § 275.6(a) states "The Commission shall exercise its regulatory authority to maintain the California High Cost Fund-A Program to provide universal service rate support to small independent telephone corporations in amounts sufficient to meet the revenue requirements established by the commission through rate-of-return regulation in furtherance of the state's universal service commitment to the continued affordability or widespread availability of safe, reliable, high-quality communications service in rural areas of the state."

<sup>91</sup> D. 95-07-054, Order Instituting Rulemaking on the Commission's Own Motion into Competition for Local Exchange Service.

<sup>92</sup> D.95-07-054, 11.

competition on separations and settlement revenues, toll and access charges, and on the High Cost Fund must first be considered through hearings. No such hearings were held and those issues were not considered in D.95-07-05 which was limited to competition in areas served by Pacific Bell and GTE. Neither the scope of D.95-07-054 nor its ordering paragraphs analyzed or addressed the issues of whether areas served by RLECs should be opened to competition.

D.95-07-05 does not dictate this Commission's action in the current OIR, R.11-11-007, or set precedent that may be considered in this decision. D.95-07-05 was confined to the facts specific to the areas served by Pacific Bell and GTE, and the policy choices made for those regions do not bind this Commission's consideration of the effect of competition in areas served by Small ILECs. The Commission is not bound by its precedents, but may, and indeed, must consider the current state of the facts and law relevant to considering competition in areas served by Small ILECs, an issue not considered within the scope or ordering paragraphs of D.95-07-05.

Similarly, in 1997 in D.97-09-115, the Commission opened to competition from CLECs the areas served by Roseville Telephone Corporation, now known as Surewest, and by Citizens Telephone Corporation, now known as Frontier.<sup>93</sup> While CALTEL and CCTA argued repeatedly that D.97-09-115 established Commission policy to open all areas of California to competition, that proceeding applied only to competition in areas served by Roseville Telephone and Citizens Telephone. Whether or not to open the areas served by Small ILECs to

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<sup>93</sup> D.97-09-115 (1997), Order Instituting Rulemaking on the Commission's Own Motion into Competition for Local Exchange Service; D.95-07-054, Order Instituting Rulemaking on the Commission's Own Motion into Competition for Local Exchange Service.

competition was not addressed in the findings of fact, conclusions of law, or ordering paragraphs of D.97-09-115, which did not consider Small ILEC competition within its scope.

D.97-09-115 also noted the rural telephone company exemption for interconnection or provision of network or service elements in its first footnote: “Section 251(f)(1) of the Act, however, grants an exemption from the requirements of Section 251(c) for “rural telephone companies” until they receive a “bona fide request” for interconnection, service or network elements, and the state commission determines that the exception should be terminated. Section 251(f)(2) permits LECs with fewer than 2% of the nation’s access lines to petition a state commission for suspension or modification of the requirements of Section 251(b) and (c).

As noted above, no request for such an exemption, nor any bona fide request for interconnection, service or network elements of a Small ILEC has been filed since the ’96 Act or D.97-09-115. The Commission recognized in 1997 in D.97-09-115 that the competition and interconnection policies it adopted with regard to Roseville Telephone and Citizens Telephone did not apply to Small ILECs that may be subject to a rural exemption under federal law.<sup>94</sup> Thus, D.97-09-115 does not require this Commission to open areas served by Small ILECs to competition, interconnection, or mandate provision of service or

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<sup>94</sup> D.97-09-115, n. 1., “Section 251(f)(1) of the Act, however, grants an exemption from the requirements of Section 251(c) for “rural telephone companies” until they receive a “bona fide request” for interconnection, service or network elements, and the state commission determines that the exception should be terminated. Section 251(f)(2) permits LECs with fewer than 2% of the nation’s access lines to petition a state commission for suspension or modification of the requirements of Section 251(b) and (c).”

network elements, and recognizes that federal law creates a process for rural telephone companies to seek an exemption.

Public Utilities Code Section 709.5 also requires this commission to act to ensure that “competition in telecommunications market is fair and that the state’s universal service policy is observed.” In this proceeding, R.11-11-007, we have evaluated the effect of competition on universal service, and have concluded that more specific, Small ILEC service territory analysis is necessary before definitively concluding whether competition would respect or undermine the state’s universal service policy, and other policies including public safety, reliability, just and reasonable rates, and the economic impact on telecommunications users and the High Cost A Fund in the areas the Small ILECs serve.

We make a preliminary conclusion to decline to open the areas served by RLECs to competition beyond what they current face at this time, in light of the need for continued support from the CHCF-A Fund to achieve universal service objectives and the broadband network deployment goals of Section 275.6. We note that many RLECs are currently subject to competition from wireless providers and cable companies, though service is not ubiquitous across RLEC territories. This preliminary conclusion is supported by the available record, and will be reassessed by the facts revealed in the Broadband Networks and Universal Service studies submitted in Phase 2 of this proceeding.

At the PPH in Jackson, California, several people who lived in areas outside the boundaries of the RLEC territory testified that they wanted to be served by the RLEC in light of the good voice and broadband service the RLEC provides to subscribers, and the lack of comparable service provided by ILECs. Many speakers at the Yreka, North Fork, and Jackson PPHs testified about the focus of

the RLECs on their small, rural communities, and the importance of reliable service in areas where inclement weather is common, and population is less dense. At all party meetings during the PPHs, we observed areas served by RLECs that in some places lacked access to commercial electric power, where the RLEC went to great lengths to serve customers who relied on a combination of solar and diesel power. While voice service is widely deployed in areas served by RLECs, there are still gaps in some areas, indicating a need for continued support for universal service, public institution, and public safety deployment. Several speakers at the Yreka, North Fork, and Jackson PPHs spoke about the importance of broadband service to their economic livelihood and safety, and supported RLEC work to deploy broadband capable networks to their homes, businesses, and rural institutions such as volunteer fire departments.

We ~~find~~make a preliminary finding, subject to analysis of the Broadband Networks and Universal Service studies to be conducted in Phase 2 of this proceeding, that areas served by the CHCF-A carriers are still not ripe for wireline competition. The unique characteristics of these territories including, mountainous and hilly terrain makes providing service in these areas challenging. As the Small ILECs have pointed out, they are COLRs in their territories and thus must provide a high and robust level of service to all of their customers. It is unlikely that any carrier entering a Small ILECs' service territory would seek to serve all customers in that territory through robust and reliable technologies suitable to the difficult terrain, population density, weather and other characteristics of many RLEC territories. As the Small ILECs note, it is more likely that a new provider would seek to "cherry pick" business customers and residents of denser population centers, or serve them through means that provide less high-quality and reliable service than the RLECs currently offer.

As pointed out by the Small ILECs, wireline competition would drain customer business for easier to serve and more urbanized customers. This would leave behind residential, small business, and community anchor institution customers in more scattered and harder to serve areas of the rural carrier's territory. Consequently, wireline competition would be expected to adversely affect the bulk of the hard-to-serve and high cost customers, exactly those the A-Fund is intended to protect, from receiving high-quality, reliable service at affordable rates. This would also result in the Small ILECs losing revenue and needing to seek a larger draw from the CHCF-A program.

We note that many of the areas served by RLECs were affected by wildfire in 2014, and many are in high wildfire danger areas. Universal, reliable, affordable service is critical to public safety and benefits the state as a whole.

Big River Telephone CEO Gerard Howe testified that Big River provides voice service in several markets in the country and holds a CPCN to provide service in California that does not include Small ILEC-served areas.<sup>95</sup> Mr. Howe testified that where Big River provides wholesale VoIP service to a cable company, if that cable provider wanted to provide voice outside of its cable footprint to other areas in a Small ILEC service boundary, Big River can provide that service through Hughes Satellite or through wireless Long-Term Evolution service.<sup>96</sup>

The FCC's 2014 Measuring Broadband America Report found that while satellite service is improving and new generation satellites have decreased

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<sup>95</sup> Evidentiary Hearing, 11-11-007, Sept. 4, 2014 at 828, Testimony of Gerald Howe.

<sup>96</sup> Id. at 825-826.



latency (signal delays), latency is still higher than for terrestrial services, caused by the signal traveling, at the speed of light, to the satellite and back.<sup>97</sup> In this proceeding's Evidentiary Hearings, Mr. Thompson testified that on-the-ground conditions such as canyons, tall trees, snow, valleys, and the need for a clear view of the southern sky to communicate with the satellite orbiting the equator, limit a user's ability to access a satellite signal, and often affect the quality of the signal when it can be obtained.<sup>98</sup>

These conditions are frequently found in many of the mountainous areas served by California's Small ILECs. At the PPH held in the North fork, in the area served by Sierra Telephone, Melanie Barker, President-elect of the Yosemite Gateway Association of Realtors testified that to get Internet through Hughes Net satellite you have to "have a view to the southern sky or it doesn't happen. My business partner was one of those people for a very long time and she was thrilled when she got DSL. It snowed and she didn't have any Internet. Those are very real issues."<sup>99</sup> DSL is available from Sierra Telephone's affiliate.<sup>100</sup>

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<sup>97</sup> FCC, MEASURING FIXED BROADBAND, CONSUMER WIRELINE BROADBAND PERFORMANCE IN THE UNITED STATES (2014),  
<http://www.fcc.gov/encyclopedia/measuring-broadband-america-measuring-fixed-broadband> (last visited Sept. 6, 2014); CPUC Order Instituting Rulemaking into the Review of the California High Cost Fund-A Program, Evidentiary Hearing, R. 11-11-007, 742-743 (Sept. 4, 2014) (testimony of Larry Thompson, satellite and telecom network engineer)(on file with the author) [hereinafter *CPUC High Cost Fund-A hearing, Thompson testimony*].

<sup>98</sup> CPUC High Cost Fund-A hearing, Thompson testimony, supra note 97, at 745, 749-751 (testifying that satellite service is affected by the need for a clear view of the southern sky, valleys, mountains, trees, pine needles, rain, snow, wind, solar flares, and other factors that interfere with satellite signals or make them inaccessible. Thompson also testified that satellites providers often impose monthly data caps "and slow you down substantially once you hit your cap.")

<sup>99</sup> California High Cost Fund-A Program, Public Participation Hearing, R. 11-11-007, pgs. 30-31 (April 17, 2014) (North Fork, California) (statement of Melanie Barker).

<sup>100</sup> Id. at 30.

Public safety agencies including woodland fire fighters use GIS-based maps to get near real-time data about the fire, wind, lightning, evacuations, resources, populations and facilities at risk, and can use those maps to track people and secure fire-fighting tools such as helicopters.<sup>101</sup> In areas without cell phone service and where satellite service does not work due to the terrain or lack of a clear view of the southern sky, the lack of communications infrastructure adds to fire risks, fire-fighting costs and challenges, delays incident response, and decreases public safety.

The California Department of Forestry and Fire Protection, Cal Fire, is charged with “fire protection and stewardship of over 31 million acres of California's privately-owned wildlands...and provides varied emergency services in 36 of the State's 58 counties via contracts with local governments.”<sup>102</sup> During major fires in wildland areas, Cal Fire has designated relay teams of people to gather information in the fire zone, drive out to get a cell phone signal to upload new ground-based information about the fire, order helicopters and fire-fighting resources, download updates, then drive back to the fire zone to pass on information and send someone back out to repeat the round-trip cell phone access run.<sup>103</sup> Many Small ILECs provide backhaul service to wireless carriers so

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<sup>101</sup> See e.g., *GIS Helps Response to California Fires*, ARC NEWS Online (Fall 2007), <http://www.esri.com/news/arcnews/fall07/articles/california-fires-gis-helped.html>; *Fire/GIS Software Support Tools*, NATIONAL WILDFIRE COORDINATING GROUP, GEOSPATIAL SUBCOMMITTEE, (March 17, 2014), [http://gis.nwcg.gov/links\\_tools.html](http://gis.nwcg.gov/links_tools.html).

<sup>102</sup> *About Cal Fire*, CAL FIRE, <http://calfire.ca.gov/about/about.php> (last visited Sept. 14, 2014).

<sup>103</sup> Robert Tse, Community Planning and Development Specialist, USDA-Rural Development, Panelist, CPUC Communications-Water/Energy Nexus Workshop: Panel on **Forest, Public Safety, Water Management, Bio-fuels & Water** (September 10, 2014) (describing U.S. Forest Service and Cal Fire establishing tag teams to drive out of fire zones to be able to access broadband internet to submit and

*Footnote continued on next page*

this problem may be less prevalent in certain portions of Small ILEC areas, but wireless service is spotty as the public observed at the hearings in this proceeding.

The lack of consistent and widespread wireless service in the areas served by Small ILECs was brought up over and over again in the PPHs in this proceeding. Chris McCullough stated at the Yreka, California PPH, “We have zero cell phone service on the Salmon River. We don’t get one bar or two bars – no service all the time. Landlines are the only way that we will ever be able to have phones.”<sup>104</sup> At the North Fork PPH in Sierra Telephone’s area, Melanie Barker stated that cell phone is available there on “a limited basis,” and she encouraged someone to text her since she wasn’t sure if she could get a voice call in North Fork.<sup>105</sup> Rick Peresan, Mariposa County Technical Director, stated at the North Fork PPH that losing cell service is well documented in the Sierra Telephone area and stated, “we have very limited airless coverage that really challenges our public safety. We can’t deploy mobile communications in our sheriff’s vehicles. It’s very difficult because of the terrain to expand our reach for services, especially in the area of public health, behavioral health and public

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download fire information and order resources for fire-fighting), available at <http://www.cpuc.ca.gov/NR/rdonlyres/12E1663F-51B0-4BB0-A438-47C68362CD48/0/USDA.pdf>.

<sup>104</sup> CPUC High Cost A-Fund OIR, 11-11-007, Yreka PPH, pg. 145. See also California High Cost Fund-A Program, Public Participation Hearing, R. 11-11-007, 65 (April 21, 2014) (Jackson, California) (statement of James Cottle) (“cell phone service up here is virtually nonexistent”); *Id.* at 85 (statement of Craig Parker) (“I would have to drive to Plymouth in order to use the cell phone. So that’s about 7 miles away.”); *Id.* at 100 (statement of Ted Jagoda, town chief for the Amador Fire Protection District) (“Cell service in our area can be reliable in some areas but poor to nonexistent in others...If we have no cell service we have to go to an adjacent property looking for a landline we can use to accomplish this [communicate with the dispatch center]...The advantages of maintaining landline services are the constant dependability especially in rural areas such as where we reside.”).

<sup>105</sup> California High Cost Fund-A Program, Public Participation Hearing, R.11-11-007 at 30-31 (April 17, 2014) (North Fork, California) (statement of Melanie Barker).

safety, both Sheriff and Probation.”<sup>106</sup> Richard McQuone, Professor at Fresno State University and an architect testified that he lives in the area of Small ILEC Ponderosa Telephone, next to Sierra telephone, and depends on landline in light of limited wireless service in the area. He stated “with the new antenna for Verizon or the new tower which now at least you can actually get service down here in the middle of town [.] where we live which is about a mile-and-a-half over in another little canyon [.] It’s [the cellphone] is a nice paper weight but that’s about it. I make it clear to people when I leave the university that you need to call the landline. Otherwise they’ll see me on Monday.”<sup>107</sup>

The record in this proceeding indicates that, at this time, satellite and wireless are not reliable substitutes for wireline service in areas served by Small ILECs and are insufficient to meet universal service, public safety, and reliability goals in many small ILEC areas. The Broadband Networks and Universal Service studies conducted in Phase 2 of the proceedings should examine the viability of wireless or satellite for broadband capable service and high-quality voice service at reasonably comparable levels to urban service in areas served by Small ILECs. Analysis of the availability, service quality, function, price, limits, and barriers to deployment and use of wireless or satellite service is an important factor in analyzing the potential impact of wireline competition, interconnection, or access to network or service elements from a competitor in a Small ILEC’s area.

Through this proceeding, the Commission has considered the pleadings, hearings, and arguments about competition in RLEC areas, including public

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<sup>106</sup> California High Cost Fund-A Program, Public Participation Hearing, R. 11-11-007 at 41-42 (April 17, 2014) (North Fork, California) (statement of Rick Peresan).

comment in the PPHs in several of the rural areas served by RLECs. It is the preliminary judgment of this Commission that in considering the relevant law, facts, comments, and record, opening the areas served by California's RLECs to wireline competition is not in the public interest at this time. We believe our decision regarding competition in this context best supports deployment of robust networks, including broadband capable networks that support both voice and Internet access services in such fashion as to ensure public safety and promote universal service.

To make a final determination about whether to open some or all Small ILEC areas to competition, in Phase 2 of this proceeding, the Commission will conduct the Broadband Networks and Universal Service studies to evaluate a variety of factors that affect deployment and availability of broadband capable and high-quality voice networks. The studies will evaluate facts and issues including, but not limited to: the extent of broadband capable network build-out in the Small ILEC areas including information on speed capability and offerings, latency, data caps, and other relevant factors for broadband and high-quality voice. The studies will account for the new FCC standard under the CAF order that broadband networks eligible for federal support have speeds of 10 mbps down and 1 up, and evaluate what investments would be needed to comply with that standard, and document the extent to which Small ILEC broadband meets California's underserved standard of 6 mbps down and 1.5 mbps up.

The Broadband Networks and Universal Service studies will identify barriers to broadband capable network and high quality voice build-out

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<sup>107</sup> California High Cost Fund-A Program, Public Participation Hearing, R. 11-11-007 at 58 (April 17, 2014) (North Fork, California) (statement of Richard McQuone).

including: population density; demographic factors including income levels, business, government, and local institutions; terrain; access to electricity or reliance on diesel; environmental permits, and; other factors that affect investment in broadband capable networks. The studies will account for the cost of burying lines underground in light of weather and fire danger issues, and document the overlap between areas of high fire danger and Small ILEC territory. The studies should take account of the unique facts of each of the 13 ILEC areas and be fact specific. The studies will build on the CPUC broadband mapping efforts.

These studies will establish a baseline of conditions and inform the Commission about factors relevant to investment in broadband capable networks and consideration of any future requests for competition in the Small ILEC areas. We will initiate the state contracting process for the Broadband Network and Competition studies in first quarter 2015, with the studies to be conducted within approximately 18 months. The studies may also be informed by the data collected in the GRCs.

We will revisit the appropriateness of opening of some or all of the RLEC territories to wireline competition ~~in five years. This will~~ once the Broadband Networks and Universal Service studies are completed and considered by the Commission in Phase 2 of this proceeding. The Commission will evaluate Small ILEC GRCs concurrently with Phase 2 of this proceeding, in accordance with the rate case plan. As the GRCs are adopted, the Commission should consider the status of the study for that GRC's region. In evaluating the studies and the GRC, the Commission may decide to defer a decision about competition in that area until the end of the authorized GRC period to provide sufficient time to evaluate the effectiveness of the regulatory system we adopt in this order, including the

caps on corporate expenses, the increase in subscriber contributions, and the effect of these regulations on network deployment and service.

### **2.3. How Should the Commission Account for Federal Subsidy Changes?**

The FCC in its Intercarrier Compensation/Universal Service Fund (ICC/USF) Order<sup>76108</sup> changed many federal support mechanisms in a manner that affects the federal revenues available to RLECs who also draw from the CHCF-A Fund. The issue is how should the Commission account for federal subsidy changes in the implementation of the CHCF-A Fund. To answer this question, we address the sub-issue: can and should the Commission modify the mechanism for adjusting CHCF-A based on changes in federal funding and/or implementing changes in federal policy.

#### **2.3.1. Comments on the Rulemaking**

The Small ILECs argue that the Commission is required to account for changes in federal support in establishing CHCF-A support for the RLECs.<sup>77109</sup> They cite Section 275.6 of the Public Utilities Code (Section 275.6) requiring the CHCF-A to "supply the portion of the revenue requirement that cannot reasonably be provided by the customers of each small independent telephone corporation after receipt of federal universal service rate support."<sup>78110</sup> They argue that inclusion of the High Cost Loop Support (HCLS) in intrastate revenue requirements results in a smaller draw on CHCF-A.<sup>79111</sup> The Small ILECs

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<sup>76108</sup> *In the Matter of Connect America Fund*, WC Docket No. 10-90, FCC 11-161.

<sup>77109</sup> Small ILECs Opening Brief, 104:18-19.

<sup>78110</sup> *Id.*, 104:20-22.

<sup>79111</sup> *Id.*, 105:21-28.

conclude that consistent with the statutory mandate, the CHCF-A must account for any changes in federal support to fulfill the Small ILECs revenue requirement.<sup>80112</sup>

ORA contends that the CHCF-A- should not make up the difference between the Small ILECs revenues and fluctuations in federal support, without regard to the reason for fluctuation.<sup>81113</sup> ORA offers the example of the FCC's phase-in adjustment for Intercarrier Compensation and ~~High-Cost Loop Support~~<sup>HCLS</sup>, which was designed to induce carrier efficiency, and therefore should not trigger an increased recovery from CHCF-A.<sup>82114</sup> ORA points to another example of the Connect America Fund High-Cost Universal Service Support which aims to limit carriers' total eligible recovery.<sup>83115</sup> ORA concludes that CHCF-A subsidies should not be automatically increased to cover the decrease in federal subsidies for corporate expenses.<sup>84116</sup>

### **2.3.2. Discussion**

We recognize the reality of fluctuation of federal subsidies. In accounting for federal subsidy changes, the Commission seeks to remedy disruptions caused by subsidy changes, while honoring the policy objectives of federal subsidy decreases where they are consistent with the objectives of the CHCF-A. To balance multiple objectives, we propose to enact a two-prong test to determine

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<sup>80112</sup> *Id.*, 106:10-12.

<sup>81113</sup> ORA Reply Brief, 44.

<sup>82114</sup> *Id.*

<sup>83115</sup> *Id.*

<sup>84116</sup> *Id.*, 45.



whether to account for federal subsidy changes. Such a test would be applied in GRCs. The Commission will allow additional draw on CHCF-A in the face of decreased federal subsidy where two criteria are met: (1) the company has observed the federal cap on per line expenses where possible,<sup>85117</sup> unless doing so would supplement high cost support, and (2) the company's investments meet the "one network" criterion of serving to support both voice and broadband deployment.

As to the first prong, corporate expense amounts above what is allowed as a result of FCC's updated 11-161 federal formula<sup>86118</sup> must be justified by the carrier and are subject to full review in the GRC. Section 275.6(c) requires the fund to offer support in "an amount sufficient to supply the portion of the revenue requirement that cannot reasonably be provided by the customers of each small independent telephone corporation after receipt of federal universal service rate support." This Section also declares that support should include "all reasonable investments." In essence, this Section implicitly acknowledges the need for CHCF-A to account for changes in federal support, while also requiring that investments be reasonable. This first prong accomplishes both by allowing for support in light of subsidy changes, but also ensuring reasonable investment and economic efficiency by pegging them to the federal cap on per line expenses.

As to the second prong, this decision acknowledges and promotes the "one network" theory of the telecommunications industry. Copper and fiber are increasingly interconnected media, broadband based on a hybrid copper-fiber

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<sup>85117</sup> See *In the Matter of Connect America Fund*, WC Docket No. 10-90, FCC 11-61 at 210; see *supra* 2.1 for more analysis on limiting corporate expenses.

<sup>86118</sup> 47 C.F.R. 36.621(a)(4)(ii).

media is becoming an increasingly important aspect of customers' existence, and there is no reason why investments cannot support both voice and broadband to meet this demand whatever the media. Further, Public Utilities Code Section 275.6(c)(6) requires that the Commission include in the rate base "all reasonable investments necessary to provide for the delivery of high-quality voice communication services *and* the deployment of broadband-capable facilities." The inclusion of broadband deployment Section 275.6 speaks to its importance, and underlies the reason for including broadband deployment in the second prong of the Commission's test for additional draw in the face of decreased federal subsidies. ~~This additional~~In cases of investment ~~cannot be~~ for broadband service purposes only ~~and must also offer some benefits for providing high-quality voice service,~~ there will be a presumption that such investment fails the second prong, which can be rebutted by showing that recovery is appropriate in that particular situation. The purpose of the rebuttable presumption is to reinforce the Commission's intent to use the A-Fund revenues to build broadband capable networks that also support voice, yet provide flexibility for the Commission and parties in unique situations.

#### **2.4. What Metrics Should Be Used to Develop Basic Rates?**

The issue is what metrics should be used to develop Basic Residential Service Rates (basic rates) in small ILECs territories. In the Amended Scoping Memo, we identified two sub-issues that would help address this issue: 4(A) sought proposals to establish metrics for basic service rates, while 4(B) asked how should basic rates be determined if parties agree that rates can no longer be based on AT&T rates. In deciding upon these issues, we factored the need to ensure that federal subsidies continued, that A-Fund subsidies continue as mandated by the

legislature, and rural customers pay a reasonable rate. Section 275.6 requires reasonably comparable rates for A-Fund subscribers to those paid by urban telephone subscribers. D.91-09-042 determined that rates shall not exceed the target level of 150% of comparable California urban rates. The issue is whether CHCF-A Fund rates should continue to be pegged to 150% of urban rates, or whether a different rate structure should be adopted.

#### **2.4.1. Comments on the Rulemaking**

Historically, CHCF-A Fund rates have been tied to AT&T's rates. Parties agree that AT&T rates can no longer be used to determine basic rates because AT&T's rate design is no longer subject to regulatory reasonableness review.<sup>87119</sup> Additionally, Small ILECs state that pegging their rates to AT&T rates results in unreasonably high rates and is inconsistent with the Commission's ratemaking procedures.<sup>88120</sup>

TURN suggests using the FCC's benchmark linked to Access Recovery Charges (ARC) as the benchmark for Small ILEC rates.<sup>89121</sup> The TURN proposal would cap the customer's total bill at \$30; TURN understands the \$30 ARC cap to include all charges.<sup>90122</sup> ARC is an end-user charge that is designed to recover a portion of switched access revenues that have been frozen and are being phased out by 5% per year.<sup>91123</sup> These switched access revenues include interstate

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<sup>87119</sup> TURN Opening Brief, 36; Small ILECs Opening Brief, 107:4.

<sup>88120</sup> Small ILECs Opening Brief, 107:9.

<sup>89121</sup> TURN Opening Brief, 36.

<sup>90122</sup> *Id.*

<sup>91123</sup> See 47 C.F.R. 51.917.

terminating switched access, intrastate terminating switched access and net reciprocal compensation.<sup>92124</sup> ARC is an optional charge; carriers do not have to assess.<sup>93125</sup> If a carrier chooses to collect ARC, then it must comply with the FCC's rate ceiling, which is \$30.<sup>94126</sup>

ORA also proposes using the FCC ARC \$30 residential rate ceiling as a benchmark to set residential rates.<sup>95127</sup> ORA suggests \$30 as a strict ceiling so as to avoid significant and harmful effects to rural customers; especially low income customers.<sup>96128</sup>

Small ILECs do not believe end-user rates should be raised at this time. If raised, they recommend using the ARC ceiling to establish a \$30 rate that includes the subscriber line charge and all state and federal taxes and surcharges plus extended area service charges.<sup>97129</sup> Like ORA, Small ILECs believe any raise should be done on a company-specific basis.<sup>98130</sup>

Aside from developing a basic rate, parties also discuss rate adjustments. TDS Telecom argues that small ILECs need to be able to implement rate floor changes quickly to avoid losses in federal funding.<sup>99131</sup> Small ILECs recommend

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<sup>92124</sup> *Id.*

<sup>93125</sup> *Id.*

<sup>94126</sup> 47 C.F.R. § 51.917(e)(6)(iii) ("The ARC . . . may not be assessed to the extent that its assessment would bring the total of the Rate Ceiling Component Charges above the Residential Rate Ceiling.").

<sup>95127</sup> ORA Reply Brief, 46.

<sup>96128</sup> *Id.*

<sup>97129</sup> Small ILECs Opening Brief, 107:26-28.

<sup>98130</sup> Small ILECs Opening Brief, 109:1-3; ORA Reply Brief at 45.

<sup>99131</sup> TDS Telecom Reply Brief, 2:8-9.

adjusting rates according to the Gross Domestic Product Price Index (GDPPI),<sup>100132</sup> but TURN rejects this proposition by arguing that the GDPPI discussion is not present in the record and therefore should not be adopted in the proposed decision.<sup>101133</sup>

#### **2.4.2. Discussion**

We determine that it is reasonable to ~~raise the~~set a new basic rate floor and basic rate ceiling for the Small ILECs ~~to \$30, exclusive of additional charges.~~ The basic rate floor will be \$30, inclusive of additional charges. The basic rate ceiling will be \$37.00 inclusive of additional charges. This rate range of \$30.00 to \$37.00 will be presumptively reasonable. For the purpose of determining draws from the CHCF-A Fund, it will be presumed that companies are charging a basic rate of at least \$30.00. Actual rates will be set in the individual GRCs of the Small ILECs. The Small ILECs note in their brief that the current basic residential rates are set at \$20.25 pursuant to each ~~companies'~~company's last rate case, ~~and;~~ with all applicable surcharges and fees, rates are currently \$~~28.83.~~<sup>102</sup> ~~If we created a strict~~28.83. By requiring a \$30 ~~ceiling~~floor, inclusive of all surcharges and fees, the minimum total ~~would amount to a maximum~~ rate increase ~~of~~will just over a dollar. While Public Utilities Code Section 275.6 calls for reasonably comparable rates to urban telephone corporations, the statute also ensures that support is not excessive so that the burden on all state-wide contributors to the CHCF-A

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<sup>100132</sup> Small ILECs Opening Brief, 108:21-23..

<sup>101133</sup> TURN Reply, 40.

<sup>102</sup> ~~Small ILECs Opening Brief, 108:2.~~

program is ~~limited.~~<sup>103</sup>measured. Given the 2019 CHCF-A sunset date approved by the California legislature, it is reasonable to ~~raise the rate in stages; and given the need to avoid~~provide a range for basic rates, to be determined in individual GRCs, with a presumptively reasonable floor and ceiling. This avoids excessive draws on the A-Fund and ~~also to meet~~meets the urban/rural rate comparability criterion, ~~it is reasonable to adopt basic rate increases of more than a dollar~~as well as provides guidance in GRCs and notice to customers.

The ARC benchmark, exclusive of surcharges, is appropriate as a benchmark to develop basic rates. The federal government has indirectly designated \$30 as a reasonable rate by capping rates at \$30, ~~in order for~~30 when telephone corporations ~~to~~ charge the ARC. By adopting this rate as a ~~target~~floor, the Commission is acting consistently with this federal ~~designation~~guidance. The \$30 basic rate ~~must be exclusive of any additional~~(inclusive of all charges) must be the rate floor because, as mentioned above, the rates must ~~increase in order to avoid placing the~~balance a fair and reasonable burden on state-wide A-Fund contributors with a fair and reasonable rate for Small ILEC customers. Further, by setting a rate ceiling of \$37.00, even though total rates, including surcharges and fees, will surpass the \$30 ARC benchmark, which would necessarily exclude the Small ILECs ability to apply the ARC to customer bills, it would not change federal subsidies received by the ~~small~~Small ILECs because ARC is paid by customers and not the government. Because the range new basic ~~rate~~rates will be in line with federal designations, and because the rate increase will not affect the

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<sup>103</sup> ~~Pub. Util. Code § 275.6(c).~~

federal subsidies received by Small ILECs, it is reasonable to adopt the \$30 to \$37.00 rate, ~~exclusive~~ range, inclusive of surcharges and fees.

The \$30 to \$37.00 basic rate, ~~exclusive~~ range, inclusive of surcharges and fees, is also the appropriate rate based on the 150% ~~Principle-Comparability Standard. Public Utilities Code~~ Section 275.6 requires reasonably comparable rates to urban telephone corporations. A prior Commission decision, D.91-09-042, helps inform what might be reasonably comparable. That decision proclaimed that rates shall not exceed the target level of 150% of comparable California urban rates. According to basic rate data on file at the ~~Commission, the current urban basic service rate average is \$21.25, which is likely to increase each successive year. This average is based basic rates charged by the state's largest telephone providers~~ Commission, the Uniform Regulatory Framework or URF carriers (AT&T, Verizon, SureWest and Frontier): average is \$21.25. Since the URF carrier rates are uncapped, the urban basic rates have been increasing steadily since the since the Commission unfroze them as of January 1, ~~2011~~ 2011 and are likely to increase each year. Even if the current urban rate were to stay at the present rate over the next several years, the \$30 to \$37.00 basic rate ~~figure~~ range we propose for the Small ILECs would be within the 150% range of the urban rate as previously designated by the Commission. ~~Because the urban rate can be expected to increase over the next five years the proposed basic rate of \$30 will be well within the 150% target set by the Commission.~~

The increase to the \$30 ~~Basic Residential Service Rate, exclusive of other charges, will be achieved incrementally over five years. The rates will increase by 20% each year from the current rate to the \$30 rate. For example, the average current rural rate of \$20.25, would increase \$1.95 per year for each of the next five years until arriving at the \$30 rate in 2020. It is appropriate to move incrementally~~

~~for two reasons. First, we recognize that an immediate shift to the \$30 figure could be quite disruptive to rural customers, especially low income customers. A staged increase will allow customers to ease into higher rates, and ensure universal service. Second, the five year staging coincides with the four year extension of CHCF-A starting in 2015. The additional year offers a buffer in case CHCF-A is again extended beyond 2019. Because the staged rate increase to \$30, appropriately balances countervailing interests, there is no need for additional rate adjustment mechanisms.~~ to \$37.00 Basic Residential Service Rate, inclusive of other charges, will be implemented in the individual GRCs. As TURN stated in its Reply Comments to the PD, the Commission can in a Rulemaking, at most, set a cap to the basic service rates that would then be implemented during each company's GRC.

In designing this basic rate ~~increaserange~~, we consider a variety of policy perspectives. We acknowledge the unique role rural carriers serve in meeting universal service goals, and aim to ensure sufficient support for the continued achievement of these goals. We also take note of the important role that carriers play in addressing wildfire danger, which poses a real threat in California's rural areas.<sup>104</sup> Separately, we acknowledge that, as the name "California High Cost Fund" suggests, there is a higher cost to provide commensurate service to rural versus urban customers, some of which must be borne by those customers themselves. The Commission's basic rate determination appropriately ~~integrates~~balances all of these policy rationales.

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<sup>104</sup> ~~See, e.g. <http://www.sierrastar.com/2014/08/20/69196/junction-fire-incident-update.html> (listing Sierra telephone as a coordinating agency for response to the Junction Fire. See also,~~

*Footnote continued on next page*



**2.5. Are Additional Safeguards Needed to Evaluate Investments in Broadband Capable Facilities to Ensure They Are Reasonable?**

The issue is whether additional safeguards are needed to evaluate investments in broadband capability facilities to ensure they are reasonable. In the Amended Scoping Memo, we identified two sub-issues that help address this issue: 5(A) asked if the CPUC should determine how much of the investment costs may be recovered through Small ILECs from ratepayers for high quality voice communication and the deployment of broadband capable facilities. 5(B) asks parties to explore what standards should be used to evaluate investment in broadband capable facilities.

**2.5.1. Comments on the Rulemaking**

Parties agree that the Commission should determine how much of the investment costs for high quality voice communication and the deployment of broadband capable facilities may be recovered from ratepayers. The Small ILECs acknowledge that Section 275.6 requires the Commission to ensure reasonable investments in broadband-capable facilities.<sup>405134</sup> They contend that the policy is intended to align state policies with similar federal universal service policies with respect to broadband-capable facilities.

Additionally, several of the parties addressed the applicable standards to be used in evaluating investment in broadband capable facilities. Many of the parties offered over-lapping standards of evaluation. The Small ILECs state that predetermined factors are not necessary for the Commission to assess the

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~~<http://inciweb.nwcg.gov/incident/4035/> (US Forest Service report regarding the July Complex fires that happened within Siskiyou telephone territory).~~

<sup>405134</sup> Small ILEC Opening Brief, 109:14-17.

reasonableness of broadband-capable investments, but can be useful as broad guidelines.<sup>106135</sup> The Small ILECs propose the following factors for Commission staff to use in rate cases: federal and state broadband requirements, customer demand, the presence of anchor institutions, network redundancy, public safety, and service quality.

TDS Telecom agrees with the Small ILECs that standards for evaluating investments in broadband-capable facilities must ensure that small ILECs continue to have incentives to invest in facilities that provide access to high-quality, safe, and reliable voice service and access to advanced services.<sup>107136</sup> ORA similarly recommends the following factors to evaluate broadband investment: presence of anchor institutions, a broadband take-rate minimum that forecasts expected subscribers, cost per household, redundancy, and safety needs of the area.<sup>108137</sup>

### **2.5.2. Discussion**

We agree that the Commission should determine how much of the investment costs may be recovered from Small ILECs from ratepayers for deployment of broadband capable facilities that also support high quality voice communications. As to evaluation of investment, we agree with the parties that a set of factors will be useful to evaluate investment in broadband facilities. The Commission will adopt a set of factors that parties collectively agree upon. This set of factors includes: presence of anchor institutions, network redundancy,

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<sup>106135</sup> *Id.*, 110:11-14.

<sup>107136</sup> TDS Telecom Opening Brief, 1:20-23.

<sup>108137</sup> ORA Reply Brief, 46.

public safety, and service quality. [Additional factors include: regulatory requirements and customer demand.](#)<sup>138</sup> Commission staff will consider these factors when evaluating broadband-capable network investments during the Small ILECs GRCs.

## **2.6. Proposals to Establish “Fair-Market Rates” for Affiliate Use of Regulated Networks**

The issue is what proposal best establishes “fair-market rates” for affiliate use of regulated networks. To assess this issue, the Commission explores party proposals and the question of whether adjustments should be made to affiliate transaction rules for the small ILECs.

### **2.6.1. Comments on the Rulemaking**

The Small ILECs argued that it is unnecessary for the Commission to establish fair market rates for access to the small ILECs broadband-capable facilities because fair market rates have already been established by the National Exchange Carrier Association (NECA) through the NECA Tariff No. 5.<sup>109139</sup> The Small ILECs state that NECA reviews these rates annually based on cost study data collected from NECA member carriers nationwide to ensure that these rates remain fair and responsive to changing market conditions.<sup>110140</sup> They also make the argument that since access to the Independent Small LECs' broadband-capable facilities is federally designated as an interstate service, the

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<sup>138</sup> [See Comments on Proposed Decision for comments on additional factors.](#)

<sup>109139</sup> Small ILEC Opening Brief, 111:25-28.

<sup>110140</sup> *Id.*, 112:1-2.

Commission should continue to defer to NECA and the FCC in formulating fair market rates.<sup>141</sup>

The Small ILECs and TDS Telecom further contend that no changes to the affiliate transaction rules are needed at this time.<sup>142</sup> The Small LECs argue that ~~the~~ CD already oversees compliance with established robust affiliate transaction reporting rules, and no deficiency has been identified in the last twenty years of filing.<sup>143</sup>

Conversely, TURN objects to the Small ILEC argument, because “the record does not support the Small ILECs’ assertion...that NECA Tariff No. 5 contains ‘fair-market rates.’”<sup>144</sup> TURN states that cost allocation at the federal level is contentious, particularly for loop costs, and that federal rate design defies economic logic.<sup>145</sup> Instead, TURN recommends that the issue of “fair-market rates” should be taken up in individual rate cases.<sup>146</sup>

ORA found the sub-issues of “fair-market rates” and affiliate transaction rules both to be outside of the scope of ORA’s testimony.<sup>147</sup>

### **2.6.2. Discussion**

Only a few of the parties briefed this issue, and those that did devoted only a small proportion of their briefs to the issue. In light of the comments

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<sup>141</sup> *Id.*, 112:6-8.

<sup>142</sup> *Id.*, 112:12; TDS Telecom Opening Brief at 1:23-25.

<sup>143</sup> Small ILECs Opening Brief, 112.

<sup>144</sup> TURN Reply Brief, 40-41.

<sup>145</sup> TURN Reply Brief, 41

<sup>146</sup> *Id.*

<sup>147</sup> ORA Reply Brief, 46-47.

submitted and the record, the Commission will continue to use the NECA Tariff No.5 in the absence of any better alternative to encourage deployment of broadband-capable facilities. Further, we will not change the affiliate transaction rules given the apparent success of the current rules, and lack of alternative. We, however, are interested in further information on the issue of “fair-market rates” for affiliate use of regulated networks, and will plan to revisit the fair market rate issue in Phase 2.

## **2.7. Changes to Procedural Rules**

The issue is whether the Commission should change the procedural rules ~~surrounding~~associated with annual filing of CHCF-A advice letters, which would render the program more efficient.

### **2.7.1. Comments on the Rulemaking**

The Small ILECs assert that the Commission should adopt ~~the~~ CD's list of proposed procedural changes to the administration of the CHCF-A program, subject to a minor clarification.<sup>~~118~~148</sup> The Small ILECs reflect that during the workshop held in this proceeding on May 28, 2014, ~~the~~ CD and the interested parties discussed areas in the existing CHCF-A process that could be made more efficient.<sup>~~119~~149</sup>

The Small ILECs noted that CD circulated a document that contained the following three proposals : 1) to ~~change~~accelerate the due date for filing the CHCF-A advice ~~letter filing~~letters from October 1 of each year to September ~~15~~.

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<sup>~~118~~148</sup> Small ILECs Opening Brief, 113:16-17.

<sup>~~119~~149</sup> *Id.*, 113:20-21.

<sup>120</sup>15;<sup>150</sup> 2) to clarify the requirements and supporting documentation necessary for requesting funding adjustments for regulatory changes of industrywide effect;<sup>121</sup> and 3) to propose that carriers provide an accurate estimate of bookings to rate base for December when providing initial nine months actual numbers during the GRC process.

The Small ILECs requested one minor clarification to the first proposal to move the CHCF-A annual advice letter filing due date up ~~by 15 days.~~<sup>121</sup> to September 15 from October 1.<sup>151</sup> They stated that there may be limited instances where the seven months of actual data required for the means test portion of the CHCF-A filing may not be finalized by the September 15 deadline.<sup>122</sup>152 The Small ILECs explained that the October 1 filing deadline provided the Small LECs with 60 days to finalize accounts through the first seven months of the year.<sup>123</sup>153 The Small ILECs requested a modification in the interest of ensuring that the Commission receives accurate and complete information.<sup>124</sup>154 Alternatively, the Small ILECs request that the proposal be clarified to allow a company to update their means test data, by no later than October ~~1.~~<sup>125</sup>1.<sup>155</sup>

### **2.7.2. Discussion**

The Commission adopts the second and third proposals from the CHCF-A workshop. The second proposal clarifies requirements and supporting

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<sup>120</sup>150 *Id.*, 113:25—114:5.

<sup>121</sup>151 *Id.*, 114:7-9.

<sup>122</sup>152 *Id.*, 114:9-12.

<sup>123</sup>153 Small ILECs Opening Brief, 114:12-13.

<sup>124</sup>154 *Id.*, 114:16-19.

documentation for requesting funding adjustments, while the third proposal requires carriers to provide accurate estimates of bookings for rate base for December when providing initial nine months actual numbers during the rate case process. The workshop funneled the best ideas for improving the funding process from the Commission's CD, and we find the above proposals to satisfactorily improve the funding process.

As to the first proposal regarding changing the filing date from October 1 to September 15, the Commission adopts the September 15 filing date as proposed by CD. The Commission also adopts a limited extension for submission of actual and means test data upon showing of good cause, which may be granted as long as the ~~means test~~ data is submitted to CD as soon as practical after receiving the data, but no later than October 1. Moving the filing date to September ~~15~~15 allows CD to begin analytical work and the Resolution writing process earlier, leading to a more efficient process. The reason for allowing the extension of means test data is that ~~means test data is provided by NECA and CD cannot require NECA to provide this data any sooner. The extension grant~~seven months of actual data may not be available and finalized by the respective Small ILECs by September 15. The extension request must be submitted by counsel on behalf of ~~all~~respective Small ILECs rather than individually. Likewise, carriers may also submit updated respective NECA HCLS estimates on October 1.

## **2.8. California Public Utilities Code Issues**

The issue is whether there are conflicting policies in the California Public Utilities Code in regards to CHCF-A, and how can those conflicts be resolved.

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<sup>125</sup>155 *Id.*, 114:19-20.

The issue is broken down into two sub-issues. First, what is the impact of California Public Utilities Code Section 710 (Section 710) on CHCF-A carrier regulatory obligations? Second, should CHCF-A carriers receive subsidy money if they change basic service offerings to rely on IP-enabled technologies, and what is the appropriate relationship between Section 275.6 and Section 710.

### **2.8.1. Comments on the Rulemaking**

The parties generally agree that Section 710 has no impact on CHCF-A carrier regulatory obligations. TURN and other parties point out that none of the current CHCF-A recipients currently offer retail interconnected VoIP services or any other service that would fall under Section 710, so Section 710 currently has no impact on carrier obligations.<sup>126156</sup>

As to the role of subsidies for IP-enabled technologies and the appropriate relationship between Section 275.6 and Section 710, the parties agree that Section 275.6 would control over Section 710.<sup>127157</sup> ORA comments that if a carrier rejects the Commission's jurisdiction, that carrier would be ineligible for CHCF-A support.<sup>128158</sup> ORA further states that to the extent that an CHCF-A carrier's broadband-capable facilities are used to provide VoIP, Section 275.6 would supersede any impact Section 710 might have on the Commission's jurisdiction to administer CFCF-A for that carrier.<sup>129159</sup> ORA finally states that the issue is not

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<sup>126156</sup> TURN Opening Brief, 37-38; Small ILECs Opening Brief, 115:17-20.

<sup>127157</sup> TURN Opening Brief at 38; Small ILECs Opening Brief 115:13-21; ORA Reply Brief at 47; TDS Telecom Opening Brief at 1:25-26.

<sup>128158</sup> ORA Reply Brief, 47.

<sup>129159</sup> *Id.*



relevant at this time because none of the Small LECs stated that they provide VoIP services.<sup>130160</sup>

TURN states that Section 275.6 requires CHCF-A recipients to operate under rate of return regulations, comply with rate regulations, maintain carrier of last resort obligations, and remain generally subject to “the commission’s regulation of telephone corporations.”<sup>134161</sup> TURN opines that these requirements are directly in conflict with any services offered by a carrier that hopes to have these requirements preempted under Section 710, and because the provisions of Section 275.6 are more narrowly focused on CHCF-A carriers, these provisions would control over Section 710.<sup>132162</sup> Additionally, TURN declares the record, the law, and current public policy do not support expanding CHCF-A subsidies to carriers that rely on Internet Protocol (IP) Enabled technology for basic service offerings.<sup>133163</sup> TURN continues offering that no party to this docket supports such an expansion and the record does not reflect a basis upon which to justify the increase in surcharges and the reduced regulatory control over the CHCF-A supported services.<sup>134164</sup>

TURN draws a distinction between carriers, describing first the companies offering untariffed and unregulated, retail interconnected IP Enabled or VoIP service to the public, who argue that these non-tariffed VoIP services are not

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<sup>130160</sup> *Id.*

<sup>134161</sup> TURN Opening Brief, 38.

<sup>132162</sup> *Id.*

<sup>133163</sup> *Id.*

<sup>134164</sup> *Id.*

subject to Commission jurisdiction.<sup>135165</sup> TURN states that these carriers should not be provided CHCF-A subsidies, and contrasts them with carriers that are modernizing their networks to incorporate IP facilities and equipment to improve service quality and enhance services “behind the scenes.”<sup>136166</sup> TURN observes that these other companies do not make changes to the terms and conditions of the customer’s tariffed, local basic service, nor do they request preemption for their services or other obligations.<sup>137167</sup> TURN suggests that the Commission should treat these two very different scenarios differently and continue to provide CHCF-A subsidies to carriers offering services in this later scenario.<sup>138168</sup>

### **2.8.2. Discussion**

As to the issue of the impact of Section 710 on CHCF-A carrier regulatory obligations, we conclude that Section 710 has no impact on such obligations. The current CHCF-A recipients do not currently offer VoIP services, so Section 710 which governs VoIP services, would not currently impact the CHCF-A carrier regulatory obligations.

As to the issue of the relationship between Section 710 and Section 275.6, the Commission agrees that Section 275.6 supersedes Section 710 and proposes a methodology of providing CHCF-A subsidies based on the tariff status of the services offer by the A-Fund companies, and their status as rate-of-return providers subject to GRC reviews, not the technologies that may be incidentally

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<sup>135165</sup> TURN Opening Brief at 38-39.

<sup>136166</sup> *Id.*

<sup>137167</sup> TURN Opening Brief at 39.

<sup>138168</sup> *Id.*

employed to provision tariffed services. As a practical matter, because none of the CHCF-A carriers are currently providing VoIP services, Section 275.6 prevails because Section 710 does not apply without the presence of VoIP services. If a carrier provided VoIP services as an unregulated and untariffed entity under Section 710, it would fail to adhere to CHCF-A requirements, including rate of return regulation, so the carrier would not be eligible to receive subsidies, and so Section 275.6 prevails over Section 710.

If a company contends it is not offering service as a regulated Telephone Corporation, it cannot also take advantage of state subsidies. As TURN rightfully suggests, there is a distinction between untariffed, unregulated VoIP providers, and companies that submit to regulation and provision tariffed basic service.

## **2.9. All Other Issues**

All other issues presented, requested, or discussed in the briefs are outside of the scope of this decision

## **3. Comments on Proposed Decision**

The ~~proposed decision~~ Commissioner Catherine J.K. Sandoval PD of the Commissioner in this matter was mailed to the parties in accordance with ~~Section 311 of the Public Utilities~~ Pub. Util. Code § 311 and comments were allowed under Rule 14.3 of the Commission's Rules of Practice and Procedure. Comments were filed ~~on \_\_\_\_\_, and reply comments were filed on \_\_\_\_\_ by \_\_\_\_\_.~~ by CALTEL, CCTA, ORA, Small ILECs, TDS Telecom, and TURN on December 8, 2014. On December 11, 2014 Commissioner Catherine J.K. Sandoval held an All-Party Meeting regarding the Decision Adopting Rules and Regulations in Phase 1 of the Rulemaking for the California High Cost Fund-A Program. The meeting was attended by CALTEL, CCTA, ORA, Small

ILECs, TDS Telecom, and TURN. Reply comments were filed by CALTEL, CCTA, ORA, Small ILECs, and TURN on December 15, 2014.

The parties addressed issue 2.1.1 of the PD regarding broadband revenue imputation. The Small ILECs support the PD's policy conclusion of broadband revenue imputation, but argue that the PD dicta regarding imputation incorrectly states the law.<sup>169</sup> TDS Telecom contends that while the policy conclusion is correct as to broadband revenue imputation, the discussion of law is incorrect because broadband revenue imputation would violate state and federal law.<sup>170</sup> TURN contends that the record supports broadband revenue imputation, showing the impact of the affiliates on the bottom line of the regulated entity.<sup>171</sup> ORA argues in favor of a rebuttable presumption of broadband revenue imputation for each Small ILEC, exempted only if a showing of its broadband capable network is not substantially developed or deployed.<sup>172</sup> TURN reiterates the need to audit the Small ILECs affiliates to ensure proper accounting of investments and expenses.<sup>173</sup>

During the All-Party meeting, Small ILECs agreed with the conclusion of the PD regarding imputation. ORA stated that Public Utilities Code Section 275.6 allows the Commission to consider broadband revenue imputation, and that most Small ILECs have full broadband deployment, which would necessitate imputation. TURN supported ORA's proposal, but contended that the

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<sup>169</sup> Small ILECs Opening Comments on Proposed Decision at 3-4.

<sup>170</sup> TDS Telecom Opening Comments on Proposed Decision at 4.

<sup>171</sup> TURN Opening Comments on Proposed Decision at 3-4.

<sup>172</sup> ORA Opening Comments on Proposed Decision 1-3.

<sup>173</sup> Id. at 9.

Commission should at least impute from Sierra because of its size and broadband deployment. In TURN's reply comments, it reiterates its argument that the record supports imputation.<sup>174</sup>

The parties addressed issue 2.1.2 of the PD regarding reasonableness of corporate expenses. Small ILECs oppose the proposed corporate caps, and argue that if adopted the mechanics of the cap should be clarified.<sup>175</sup> ORA supports the PDs adoption of expense limits but claims the PD errs by allowing carriers to request A-Fund support above the expense limit levels.<sup>176</sup> At the All-Party meeting, ORA contended that corporate expenses are reasonable if under cap and unreasonable if over cap. Small ILECs advocated for a rebuttable presumption if over the cap, and that such caps should only be examined in rate cases. TURN took a middle approach supporting the ORA approach to corporate expenses except that there may be times when the federal cap is inappropriate. In reply comments, ORA rejects the possibility that the caps on corporate expenses have a rebuttable presumption.<sup>177</sup>

The parties addressed issue 2.2 of the PD regarding opening RLEC territory to competition. The Small ILECs support maintaining closure of RLEC territory to competition. TDS Telecom also states that the PD properly keeps RLEC territory closed to competition.<sup>178</sup>

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<sup>174</sup> TURN Reply Comments on Proposed Decision at 1-2.

<sup>175</sup> Small ILECs Opening Comments on Proposed Decision at 8-9.

<sup>176</sup> ORA Opening Comments on Proposed Decision at 4.

<sup>177</sup> ORA Reply Comments on Proposed Decision at 4.

<sup>178</sup> TDS Telecom Opening Comments on Proposed Decision at 5.

CALTEL argues that regarding competition the PD is inconsistent with the requirements of federal law and prior FCC decisions.<sup>179</sup> CALTEL states that RLECs provision of access to service elements under 47 U.S.C. Sections 251(a) and (b) enables local competition.<sup>180</sup> CALTEL draws a distinction between 47 U.S.C Sections 251 (a) and (b) on one hand, and (c) on the other, stating that CLECs have the right to request that the Commission arbitrate negotiations of interconnection agreements.<sup>181</sup> CALTEL also states that the Commission has no authority to consider issues of economic burden regarding RLECs Sections 251(a) and (b) obligations of the 1996 Act.<sup>182</sup> Finally, CALTEL argues that the Commission risks federal preemption if the PD is not modified.<sup>183</sup> In its reply comments, CALTEL reiterates the argument that federal law preempts state commission jurisdiction over competitive local market entry because RLECs are not exempt from the requirements of 47 U.S.C. Sections 251(a) and (b), and Section 251(b) requires that RLECs provide services necessary to open local market to competition.<sup>184</sup> CALTEL also contends that Small ILECs have presented no authority for the Commission to avoid preemption that is inevitable under Section 252.<sup>185</sup>

CCTA contends that the Commission is prohibited from restricting competition as a matter of law in the RLEC territories, under Sections 251(a), (b),

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<sup>179</sup> CALTEL Opening Comment on Proposed Decision at 4.

<sup>180</sup> Id.

<sup>181</sup> Id. at 8.

<sup>182</sup> Id. at 9.

<sup>183</sup> Id. at 10.

<sup>184</sup> CALTEL Reply Comments at 2-3.

<sup>185</sup> Id. at 4-5.

and (c).<sup>186</sup> CCTA continues, explaining that the PD is contrary to Section 253 and if not reversed, it will subject the Commission to federal preemption.<sup>187</sup> CCTA concludes that the PD's public interest assessment is misplaced, and its expression of public policy on competition violates the policy of the State of California.<sup>188</sup> In its reply comments, CCTA emphasizes the Rural Declaratory Ruling that provides for competitive entry and the "TWC Order" which asserts that denial of the right to interconnection is inconsistent with the 1996 Act.<sup>189</sup> CCTA further argues that Section 251(f) rural exemption from Section 251(c) requirements does not insulate rural providers from competition.<sup>190</sup> CCTA concludes its reply comments by emphasizing the likelihood of Section 252 preemption by the FCC.<sup>191</sup>

During the All-Party meeting, parties agreed that the primary issue regarding competition is the interpretation of § 251(b), and the implication of certificates of public necessity and convenience (CPCNs). The Small ILECs and CALTEL disagreed over federal rulings provide preemption of Commission discretion over competition.

In response to the parties' comments and replies, we have elaborated the legal rationale under federal and state law. We have also made a preliminary determination that the Small ILECs' territories will not be opened to wireline

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<sup>186</sup> CCTA Opening Comments on Proposed Decision at 2.

<sup>187</sup> Id. at 7.

<sup>188</sup> Id. at 9.

<sup>189</sup> CCTA Reply Comments on Proposed Decision at 2.

<sup>190</sup> Id. at 3.

<sup>191</sup> Id. at 4.

competition at this time. We will revisit the appropriateness of opening some or all of the Small ILEC territories to wireline competition after the Broadband Networks and Universal Service studies are completed and considered by the Commission in Phase 2 of this proceeding.

The parties addressed issue 2.3 of the PD regarding adjustments for federal subsidy changes. Small ILECs request that the Commission clarify the two-prong test for Small ILECs to qualify for CHCF-A adjustments based on federal subsidy decreases.<sup>192</sup> TDS Telecom claims that the PD should be modified to provide all RLECs the authority to implement rate adjustments in order to comply with FCC Local Rate Floor changes.<sup>193</sup> TURN argues in favor of revising the two-prong test to allow additional CHCF-A draw in the face of federal subsidy reduction, disfavoring automatic recovery of disallowed federal expenses, and urges treatment of expense impacts in the GRCs.<sup>194</sup> ORA contends that the test for A-Fund adjustment in light of reduced federal subsidies lacks clarity and should be revised to provide meaningful guidance to allow parties to determine whether conditions have been met.<sup>195</sup>

ORA's reply comments call for a simplification of the two-prong test for federal subsidy decreases.<sup>196</sup> Small ILEC's reply comments also call for a complete revision or at least a clarification of the test, to apply in the rate case to address reductions in federal funding and support of both voice service and

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<sup>192</sup> Small ILECs Opening Comments on Proposed Decision at 10.

<sup>193</sup> TDS Telecom Opening Comments on Proposed Decision at 1-2.

<sup>194</sup> TURN Opening Comments on Proposed Decision at 13-14.

<sup>195</sup> ORA Opening Comments on Proposed Decision at 4-5.

<sup>196</sup> ORA Reply Comments on Proposed Decision at 4.



access to advanced series.<sup>197</sup> TURN's reply comments also criticizes the two-prong test, instead advocating for standard criteria applied on a case-by-case basis.

We have reviewed the comments of the parties regarding issue 2.3 and changed the proposed decision to state that in cases of investment for broadband service purposes only, there will be a presumption that such investment fails the second prong, which can be rebutted by showing that recovery is appropriate in that particular situation. The purpose of the rebuttable presumption is to reinforce the Commission's intent to use the A-Fund revenues to build broadband capable networks that also support voice, yet provide flexibility for the Commission and parties in unique situations. The two-prong test is consistent with Public Utilities Code Section 275.6(c) by allowing for support in light of federal subsidy changes while ensuring reasonable investment, and promoting investment in broadband capable networks and high-quality voice service.

The parties addressed issue 2.4 of the PD regarding what metrics to use to develop basic rates. Small ILECs contend that the increase in basic residential service rates is unreasonably high, not reflected in the record, and may interfere with the LifeLine program.<sup>198</sup> TDS Telecom argues that the Commission should grant authority to RLECs which do not draw from the CHCF-A to adjust rates through the annual CHCF-A advice letter process to the \$30 benchmark rate.<sup>199</sup> TURN refutes the PD's basic service rate increase, stating that such a position was

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<sup>197</sup> Small ILECs Reply Comments on Proposed Decision at 3.

<sup>198</sup> Small ILECs Opening Comments on Proposed Decision at 5-6.

<sup>199</sup> TDS Telecom Opening Comments on Proposed Decision at 1-2.

not supported by the parties, is based on outdated principles, and could lead to decreased service in rural areas.<sup>200</sup> During the All-Party meeting, parties agreed that the increase to \$30, exclusive of surcharges and fees is untenable.

In reply comments, ORA states that raising the basic residential service rates from \$20.25 to \$30 is excessive, and \$30 should be a ceiling.<sup>201</sup> Small ILECs also express concern regarding the basic rate increase, criticizing the “150% Principle,” emphasizing the lack of support in the record, and stating that such an increase must be done in a ratesetting proceeding.<sup>202</sup> TURN adds to its argument against the proposed rate increase by pointing to a violation of procedural rules and rate that would be substantially higher than unregulated urban rates.<sup>203</sup>

The parties addressed issue 2.5 of the PD regarding reasonableness of broadband investments. Small ILECs argue that when considering broadband investment reasonableness, the Commission should, in a rate case, consider regulatory requirements and projected customer demand, in addition to the existing four proposed requirements.<sup>204</sup> During the All-Party meeting, Small ILECs reiterated their comments and TURN also supported the two additional factors proposed by the Small ILECs.

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<sup>200</sup> TURN Opening Comments on Proposed Decision at 5-6.

<sup>201</sup> ORA Reply Comments on Proposed Decision at 3.

<sup>202</sup> Small ILECs Reply Comments on Proposed Decision at 2.

<sup>203</sup> TURN Reply Comments on Proposed Decision at 4.

<sup>204</sup> Small ILECs Opening Comments on Proposed Decision at 11-12.

The parties addressed issue 2.7 of the PD regarding changes to procedural rules. Small ILECs request a correction of factual inaccuracies regarding the role of NECA and means test data for procedural rules.<sup>205</sup>

The parties addressed additional issues not contained within the PD. The Small ILECs call for refining the scope of Phase 2 in light of recent legal developments, and for parties to be given the opportunity to comment on the proposed rate case plan and waterfall changes before the proposals appear in a proposed decision.<sup>206</sup> TDS Telecom further argues that the scope of Phase 2 should be revised to reflect recent legislation.<sup>207</sup> ORA urges the Commission to adopt a proposed Rate Case Plan to avoid the probable necessity of extending the April 2015 deadline that would trigger A-Fund subsidy reductions.<sup>208</sup> TURN also requests clarification of Phase 2.<sup>209</sup>

#### **4. Assignment of Proceeding**

Catherine J.K. Sandoval is the assigned Commissioner and W. Anthony Colbert is the assigned ALJ in this proceeding.

#### **Findings of Fact**

1. In Order Instituting Rulemaking (R.11-11-007), the Commission began a review of the CHCF-A program.

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<sup>205</sup> Id. at 13.

<sup>206</sup> Id. at 14-15.

<sup>207</sup> TDS Telecom Opening Comments on Proposed Decision at 3.

<sup>208</sup> ORA Opening Comments on Proposed Decision at 6.

<sup>209</sup> TURN Reply Comments on Proposed Decision at 5.

2. In D.13-12-005, the Commission adopted a one-year stay in the GRC Schedule of the Small ILECs with the exception of Kerman Telephone Company and a one-year freeze in the Waterfall Mechanism.

3. D.13-02-005 allowed the stay and freeze to be extended for six months by the assigned ALJ.

4. On May 22, 2013, Commissioner Sandoval issued a Scoping Memo and Ruling.

5. On March 18, 2014, the assigned Commissioner issued an Amended Scoping Memo and Ruling.

6. The Amended Scoping Ruling revised the scope set forth in that earlier Scoping Memo, identified new issues, set forth the issues to be addressed in workshops, EH and/or briefs, and sought additional comments from the Parties; in addition, the proceeding was divided into two phases (Phase 1 and Phase 2).

7. On April 17, 2014, a PPH was held in North Fork, California.

8. On April 21 a PPH was held in Jackson, California.

9. On May 8, 2014 a PPH was held in Yreka, California.

10. On April 15, 2014, the Small ILECs submitted a letter to the Commission's Executive Director pursuant to Rule 16.6 requesting a 60-day extension to the current rate case deadline and associated waterfall mechanism.

11. The Commission's Executive Director granted the 60-day extension request on April 29, 2014, effectively extending the rate case deadline and associated waterfall mechanism to August 29, 2014.

12. In D.14-08-010 the Commission extended the current stay of the GRC schedules and freeze of the waterfall provisions for CHCF-A recipients. The stay of the GRC schedules was extended until December 31, 2014. The freeze of the waterfall provisions for CHCF-A recipients was extended to April 2015.

13. D.14-08-010 allowed for stay of the GRC schedules to be extended for three months by a ruling of the assigned ALJ if Phase 1 of this proceeding is not completed by December 31, 2014.

14. In 2012 the California Legislature passed SB 379 which is codified as Section 275.6 of the Public Utilities Code.

~~15. Section 275.6 allows the Small ILECS to include all reasonable investments necessary to provide for the delivery of high-quality communication services and the deployment of broadband-capable facilities in their rate base.~~

~~16. No state or federal law prohibits or requires broadband imputation and the decision of whether to do so is left to the Commission's judgment based on the record.~~

15. ~~17.~~ Broadband imputation is a ratemaking mechanism within the Commission's authority to regulate telecommunications companies.

16. ~~18.~~ Not all of the Small ILECs are providing or have ISPs that are providing broadband services.

17. ~~19. Small ILECs that are providing broadband directly or through their ISP affiliates are at different stages of deployment.~~ The extent and variances in deployment of broadband capable networks and high-quality voice communications service will be evaluated for each Small ILEC area in the Broadband Networks and Universal Service studies to be conducted in Phase 2 of this proceeding, and will account for service levels in light of changing federal standards for broadband.

18. ~~20.~~ In light of the record, ~~state of~~ changing federal standards for measuring whether broadband and network deployment in rural areas is reasonably comparable to urban areas, universal service and public safety objectives of federal and state law and this Commission's rules, we ~~should~~ preliminarily decide

not to impose broadband revenue imputation at this time, and for the Small ILECs that participate in the first GRC cycle following the adoption of this Decision.

19. ~~21.~~ The issue of broadband revenue imputation should be revisited in ~~five years~~ Phase 2 of this proceeding after the Broadband Networks and Universal Service studies are completed and the Commission shall determine whether to impute broadband revenues in the second or subsequent GRC cycles following this Decision.

20. The Commission's Communications Division should initiate the California state contracting process in order to commence the Broadband Network and Competition studies in the first quarter of 2015, with the studies to be conducted within 18 months of commencement.

21. ~~22.~~ ~~When the~~ The Governor ~~vetoed AB 1693, he stated~~ in his veto of AB 1693 recommended that the Commission ~~should~~ create a GRC Plan to encourage timely completion of the Small ILECs' GRCs.

~~23. The Assigned Commissioner will issue a Ruling soliciting comments in order to create a GRC Plan for the Small ILECs which will be implemented in an interim decision between Phase 1 and 2 of the instant proceeding~~

22. ~~24.~~ Adopting a universal standard for determining a reasonable level of corporate operations expenses for carriers receiving subsidies from the CHCF-A allows the program to achieve its goals while ensuring that the level of support is not excessive and an undue burden on California ratepayers who contribute to the fund.

23. ~~25.~~ The FCC's Corporate Expense Caps are a rationale mechanism for calculating and determining a reasonable level of corporate expenses for those carriers drawing from the Fund.

~~24. 26.~~ Adopting and applying the FCC Corporate Expense Caps will not limit the amount of a company's corporate expenditures but will limit the amount of corporate expenditures that can be recovered from the CHCF-A program.

25. Applying the FCC Corporate Expense Cap as a rebuttable presumption provides clarity in how the caps will operate, and offers flexibility for the Commission and parties to account for unique situations.

~~26. 27.~~ Adjustment to the Waterfall mechanism will be addressed through an ACR and interim PD between Phase 1 and Phase 2 of the instant proceeding.

~~28. Competition is an important goal in the territories covered by the CHCF-A program and federal and state law allows but does not mandate that these service areas be opened to wireline competition.~~

~~29. D.95-07-054, neither binds this Commission's action, nor provides guidance for the Commission's evaluation of whether opening the areas served by RLECs is appropriate at this time.~~

~~30. D.95-07-054 analyzed whether areas served by non-rate-regulated ILECs should be open to competition, and did not consider whether areas served by RLECs should be open to competition.~~

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~~28. 31.~~ The Small ILECs are COLRs and they are obligated to serve all the customers in their service area who request service.

~~29. 32.~~ Competitors may tend to serve only small portions of any of the Small ILECs' service areas with high quality, high reliable voice service and CLECs ~~are~~may be likely to "cherry pick" business customers rather than serve significant portions of rural service territories, particularly customers whose cost to serve is high.

~~30.~~ ~~33.~~ It is unlikely that any carrier entering a Small ILECs' service territory would seek to serve all customers in that territory through robust and reliable technologies suitable to the difficult terrain, population density, weather and other characteristic of many RLEC territories.

~~34. Neither state nor federal law mandates that the Commission open small LEC territories to competition.~~

~~31.~~ ~~35.~~ Federal subsidies have and may continue to decrease, and such decreases, including those decreases enacted by the USF/ICC Transformation Order, may be tied to increasing operational efficiency or limited corporate expenses.

~~36. California Public Utilities Code Section 275.6(c) requires CHCF A support in "an amount sufficient to supply the portion of the revenue requirement that cannot reasonably be provided by the customers of each small independent telephone corporation after receipt of federal universal service rate support."~~

~~37. Section 275.6 declares that support should include "all reasonable investments."~~

~~32.~~ ~~38.~~ The federal government has indirectly designated \$30 as a reasonable rate by capping rates at \$30, in order for telephone corporations to charge the ARC.

~~39. D.91-09-042 proclaimed that rates shall not exceed the target level of 150% of comparable California urban rates.~~

~~33.~~ ~~40. Section 275.6 requires the Commission to ensure reasonable investments in broadband-capable facilities.~~ Actual basic service rates will be determined and implemented during each company's GRC.

~~34.~~ ~~41.~~ Pre-determined factors are useful in evaluating the reasonableness of broadband-capable facilities.



35. ~~42.~~ In creating the NECA Tariff No.5, NECA reviews affiliate rates annually based on cost study data collected from NECA member carriers nationwide to ensure that these rates remain fair and responsive to changing market conditions.

36. ~~43.~~ The Commission's CD currently oversees compliance with established robust affiliate transaction reporting rules, and no deficiency has been identified in the last twenty years of filing.

37. ~~44.~~ The Commission's CD crafted procedural rule changes to make the CHCF-A process more efficient, with party input during a CHCF-A workshop.

38. ~~45.~~ Moving the CHCF-A filing date to September 15, allows CD to begin analytical work and the Resolution writing process earlier, leading to a more efficient process.

39. ~~46. Means test data is provided by NECA, and so CD cannot require NECA to provide this data any sooner. If seven months of actual data is not available and finalized by the respective Small ILECs by September 15, an extension request for submission of this data by no later than October 1 must be submitted by counsel on behalf of respective Small ILECs, rather than individually.~~

40. ~~47.~~ The current CHCF-A recipients do not currently offer VoIP services, so Public Utilities Code Section 710 which governs VoIP services, would not currently impact the CHCF-A carrier regulatory obligations.

41. ~~48.~~ If a carrier provided VoIP services as an unregulated and untariffed entity under Public Utilities Code Section 710, it would fail to adhere to CHCF-A requirements, including rate of return regulation, as set forth in Public Utilities Code Section 275.6, so the carrier could no longer receive subsidies, and Public Utilities Code Section 275.6 would prevail over Public Utilities Code Section 710.

42. Many Small ILECs are currently subject to competition from wireless providers and cable companies, though service is not ubiquitous across Small ILEC territories.

43. Wireless service in Small ILEC territories is not consistent and widespread.

44. Satellite and wireless services are not reliable substitutes at this time for wireline service in areas served by Small ILECs and are currently insufficient to meet universal service, public safety, and reliability goals in many small ILEC areas.

45. Since passage of the '96 Act, no CLEC has requested a Small ILEC for access to interconnection elements in Section 251(b) or (c) of the Act.

46. Since passage of the '96 Act, no Small ILEC has requested a rural exemption under Section 251(f) of the Act for the suspension or modification of the requirements under Sections 251(b) and (c).

47. No Small ILECs filed a petition that would require evaluation of a rural market exemption under Section 253(f).

48. CLECs and Small ILECs exchange engage in traffic exchange and call are completed under Section 251(a) of the Act.

49. No petition has been received by this Commission to change the CPCN service areas to allow for service in areas served by Small ILECs.

50. California's 13 RLECs service territories differ in terrain from mountainous to desert, have varying levels of population and visitors, differ in service costs, and have different levels of barriers to service including lack of access to electricity.

**Conclusions of Law**

1. Neither state nor federal law prohibits broadband ~~imputation~~revenue imputation and the decision of whether to do so is left to the Commission's judgment based on the record.
2. Broadband revenue imputation does not constitute a violation of the U.S. and California Constitutions as taking of property without just compensation.
3. Broadband revenue imputation is a ratemaking mechanism within the Commission's authority to regulate telecommunications companies.
4. The FCC's Corporate Expense Caps are a rationale mechanism for calculating and determining a reasonable level of corporate expenses for those carriers drawing from the CHCF-A.
5. If a carrier's actual corporate expense amounts exceed the caps, that carrier can file a request for additional support from the CHCF-A program in their GRC application.
6. Pursuant to 47 U.S.C. Section ~~254~~251(c), ILECs must negotiate in good faith interconnection agreements for the transmission and routing of telephone exchange service and exchange access and permit a requesting telecommunications carrier to interconnect to any technically feasible point in the network, subject to rural exemptions for rural companies.
7. 47 U.S.C. Section ~~254~~251(f)(1)(a) exempts ~~Rural~~rural telephone companies from the ~~Interconnection~~interconnection requirements of 47 U.S.C. Section ~~254~~251(c) "until (i) such company has received a bona fide request for interconnection, services, or network elements, and (ii) the State commission determines (under subparagraph (B)) that such request is not unduly economically burdensome, is technically feasible, and is consistent with Section 254 of this title (other than subsections (b)(7) and (c)(1)(D))."

8. Federal law does not mandate that ~~RLECs~~the Small ILECs LECs negotiate interconnection agreements of 47 U.S.C. Section 251(c) elements to facilitate local competition and the FCC has specifically recognized ~~the RLECs~~rural carriers' statutory exemption from this requirement under 47 U.S.C. Section 251(f).

~~9. Neither state nor federal law absolutely requires that the Commission open RLEC territories to competition.~~

~~9. 10. The~~We make a preliminary determination that the Small ILECs' territories should not be opened to wireline competition beyond what they current face at this time, in light of the need for continued support from the CHCF-A Fund to achieve universal service objectives and the broadband network deployment goals of ~~Pub. Util.~~Public Utilities Code Section ~~275.6-~~275.6.

~~10. 11.~~In light of statutory authority and policy objectives, it is appropriate for the Commission to allow additional draw on CHCF-A in the face of decreased federal subsidy where two criteria are met: (1) the company has mirrored the federal cap on per line expenses where possible, unless doing so would supplement high cost support, and (2) the company's investments meet the "one network" criterion of serving to support both voice and broadband deployment. In cases of investment for broadband service purposes only, it is reasonable to have a presumption that investment fails the second prong, which can be rebutted by showing that recovery is appropriate in that particular situation.

~~11. 12.~~It is reasonable to ~~raise the~~set a basic rate ~~to \$30, exclusive~~floor of \$30.00 and basic rate ceiling of \$37.00 inclusive of additional charges, because this range is consistent with the ARC benchmark ~~is appropriate as a benchmark to develop basic rates, and the \$30 rate is appropriate as based on~~and the 150% ~~Principle of~~urban rates benchmark.

12. ~~13.~~ It is reasonable to evaluate investment in broadband facilities by examining the following set of factors: presence of anchor institutions, redundancy, public safety, ~~and~~ service quality, regulatory requirements, and customer demand.

13. ~~14.~~ It is reasonable for Small ILECs to continue to use the NECA Tariff No. 5 to make rates for affiliate use of regulated networks.

14. ~~15.~~ It is currently unnecessary for the Commission to change the affiliate transaction rules.

15. ~~16.~~ It is reasonable to adopt CD's procedural rule change proposals, including clarifying requirements and supporting documentation for requesting funding adjustments, and the requirement for carriers to provide accurate estimates of bookings to rate base in December when providing the initial nine month actual numbers during the rate case process.

16. ~~17.~~ It is reasonable to adopt CD's procedural rule change proposal as modified, which changes the annual advice letter filing date from October 1 to September 15, with a limited extension for submission of seven months of actual and means test data upon showing of good cause, which may be granted as long as ~~the means test~~this data is submitted to CD as soon as practical after receiving the data, but no later than October 1.

17. Public Utilities Code Section 275.6 allows the Small ILECS to include all reasonable investments necessary to provide for the delivery of high-quality voice communication services and the deployment of broadband-capable facilities in their rate base.

18. Public Utilities Code Section 275.6(c) requires CHCF-A support in "an amount sufficient to supply the portion of the revenue requirement that cannot

reasonably be provided by the customers of each small independent telephone corporation after receipt of federal universal service rate support.”

19. ~~18.~~ Public Utilities Code Section 710 has no impact on CHCF-A carrier regulatory obligations.

20. ~~19.~~ Public Utilities Code Section 275.6 supersedes Public Utilities Code Section 710 and CHCF-A subsidies must be based on the tariff status of the company.

21. ~~20.~~ Public Utilities Code Section 710 has no impact the regulatory obligations of Small ILECS that receive CHCF-A Program support.

22. ~~21.~~ In determining a methodology of providing CHCF-A Program support Public Utilities Code Section 275.6 is predominate over Public Utilities Code Section 710.

23. The assigned Commissioner will issue a Ruling soliciting comments in order to create a GRC Plan for the Small ILECs which will be implemented in an interim decision between Phase 1 and 2 of the instant proceeding.

24. D.91-09-042 proclaimed that rates shall not exceed the target level of 150% of comparable California urban rates.

25. D.95-07-054, neither binds this Commission’s action, nor provides guidance for the Commission’s evaluation of whether opening the areas served by RLECs is appropriate at this time.

26. D.95-07-054 analyzed whether areas served by non-rate-regulated ILECs should be open to competition, and did not consider whether areas served by RLECs should be open to competition.

27. Rural exemption under 47 U.S.C. 251(f) does not remove 47 U.S.C. Sections 251(a) and (b) obligations.

28. 47 U.S.C. Section 251(a) requires telecommunications carriers to interconnect directly or indirectly with other carriers.

29. 47 U.S.C. Section 251(b) requires local exchange carriers to make available resale of its telecommunications services, number portability, dialing parity, access to rights-of-way, and establish reciprocal compensation arrangements for the transport and termination of telecommunications.

30. 47 U.S.C. Section 251(c) requires incumbent local exchange carriers to negotiate in good faith, interconnect, provide access to unbundled network elements and offer for resale of its telecommunications services at wholesale rates.

31. 47 U.S.C. Section 251(f)(2) provides a rural exemption to Small ILECs from Section 251(c) obligations until they have received a bona fide request for interconnection and the state commission has determined that such request is not unduly economically burdensome, is technically feasible, and is consistent with Section 254 of the Act.

32. 47 U.S.C. Section 251(f)(2) requires a competitor to make a bona fide request to the state commission to access to Section 251(c) elements.

33. Under 47 U.S.C. Section 253, states and local governments are generally prohibited from establishing rules that prohibit any entity to provide any interstate or intrastate telecommunication services unless the rules are competitively neutral and necessary to preserve and advance universal service, protect the public safety and welfare, and ensure the continued quality of telecommunications services and safeguard the rights of consumers.

34. 47 U.S.C. Section 253(f) allows the Commission to consider a petition for a rural market exemption.

35. 47 U.S.C. Section 214(e)(1) establishes the standards and process by which a state may designate a common carrier as an eligible telecommunications carrier eligible for universal service funding.

36. Public Utilities Code Section 709.5(a) provides a legislative intent to open telecommunications markets subject to the CPUC jurisdiction competition, and mandates that the “commission shall take steps to ensure that competition in telecommunications market is fair and that the state’s universal service policy is observed.”

37. Public Utilities Code Section 275.6, which provides the Commission with broad authority to establish and administer the A-Fund, does not require the Commission to open Small ILEC territories to wireline competition.

38. D.97-09-115 does not require the Commission to open areas served by Small ILECs to competition, interconnection, or mandate provision of service or network elements, and recognizes that federal law creates a process for rural telephone companies to seek an exemption.

39. The FCC’s 2014 Measuring Broadband America Report found that while satellite service is improving and new generation satellites have decreased latency (signal delays), latency is still higher than for terrestrial services, caused by the signal traveling, at the speed of light, to the satellite and back.

40. We preliminarily conclude that it is not in the public interest to open the Small ILECs territories to wireline competition at this time, subject to our review of the Broadband Networks and Universal Service studies to be conducted in Phase 2 of this proceeding.

41. The Broadband Networks and Universal Service studies will be conducted in Phase II of this proceeding to analyze the potential impact of competition in each Small ILEC territories on universal service, reliability, safety, just and



reasonable rates, deployment of broadband capable networks, deployment and maintenance of high-quality voice networks, and the economic impact on users of telecommunications services, and on the High Cost A Fund, and to analyze the current extent of broadband network deployment and the speeds, latency, and other characteristics of service, as well as barriers to network deployment, and factors that affect network deployment such as population characteristics, terrain, density, and businesses, in each Small ILEC area.

42. Whether to open some or all of the Small ILEC areas to competition or final disposition of any petitions for a rural exemption, to amend the service area of CPCNs to include Small ILEC-served areas, or for access to Section 251(b) elements, to authorize interconnection under Section 251(c), to provide facilities-based service in small ILEC areas with or without Section 251(b) elements or interconnection under Section 251(c), or to allow interstate and interstate telecommunications service in Small ILEC markets under Section 253 is not at issue because the requisite filings have not been submitted to this Commission, so those issues are not ripe for review.

43. Any request filed and received subsequent to this Phase I decision to amend CPCNs to include Small ILEC areas or for access to Section 251(b) elements or interconnection under Section 251 (c), or for a petition under Section 251(f)(2) to suspend or modify the application of the requirements of Section 251(b) or (c), or a petition under Section 253 (f) will be deferred until the Broadband Networks and Universal Service studies are completed in Phase 2 of this proceeding and the Commission has evaluated the study to determine in Phase 2 whether or not some or all of the Small ILEC areas should be opened to CLEC competition.

## O R D E R

## IT IS ORDERED that:

1. Broadband ~~Imputation~~revenue imputation will not be imposed on Small Incumbent Local Exchange Carriers which receive funds from the California High Cost Fund-A Program ~~any sooner than January 2020 at which time the Commission will revisit the issue.~~at this time and through the first General Rate Case (GRC) cycle following the adoption of this Decision, but may be considered in Phase 2 of this proceeding following evaluation of the Broadband Networks and Universal Service studies, for the second or any subsequent GRC cycles.
2. Small Incumbent Local Exchange Carriers which receive funds from the California High Cost Fund-A must adhere to the Federal Communications Commission's standards for corporate expense limits in their General Rate Cases.
3. If a Small Incumbent Local Exchange Carrier's actual corporate expense amounts exceed the Federal Communications Commission's corporate expenses caps, that carrier ~~can file a request for~~has the opportunity in the General Rate Case application to rebut the presumption of unreasonableness to seek additional support from the California High Cost Fund-A Program ~~in their General Rate Case application.~~Conversely, corporate expenses that fall below the cap would be presumed reasonable subject to an opportunity by other parties to rebut that conclusion in the General Rate Case.
4. The ~~Assigned~~assigned Commissioner will issue a Ruling soliciting comments in order to create a ~~GRC~~general rate case Plan for the Small Incumbent Local Exchange Carriers which will be implemented in an interim decision between Phase 1 and 2 of the instant proceeding

5. ~~The~~We make a preliminary determination that Small Incumbent Local Exchange Carrier's territories will not be opened to wireline competition ~~any~~  
~~sooner than January 2020 at which time the Commission will revisit the issue~~at  
this time, and whether wireline competition should be permitted in some or all of  
those areas will be determined in Phase 2 of this proceeding, after evaluating the  
Broadband Networks and Universal Service studies for each of the Small  
Incumbent Local Exchange Carrier's service area.

6. The Commission's Communications Division will initiate the California  
state contracting process in order to commence the Broadband Network and  
Competition studies in the first quarter of 2015, with the studies to be conducted  
within 18 months of commencement

7. Any request filed and received subsequent to this Phase 1 decision to  
amend certificates of public convenience and necessity to include Small  
Incumbent Local Exchange Carrier areas or for access to Section 251(b) elements  
or interconnection under Section 251 (c), or for a petition under Section 251(f)(2)  
to suspend or modify the application of the requirements of Section 251(b) or (c),  
or a petition under Section 253 (f) will be deferred until the Broadband Networks  
and Universal Service studies are completed in Phase 2 of this proceeding and the  
Commission has evaluated the study to determine in Phase 2 whether or not  
some or all of the Small ILEC areas should be opened to CLEC competition.

8. ~~6.~~ Small Incumbent Local Exchange Carriers may make additional draws  
from the California High Cost Fund-A Program in the event of a decrease in their  
federal subsidy where two criteria are met: (1) the Small Incumbent Local  
Exchange Carrier has mirrored the federal cap on per line expenses where  
possible, unless doing so would supplement high cost support, and (2) the Small  
Incumbent Local Exchange Carriers' investments meet the one network criterion

of serving to support both voice and broadband deployment. In cases of investment for broadband service purposes only, there will be a presumption that the investment fails the second prong, which can be rebutted by showing that recovery is appropriate in that particular situation.

9. ~~7.~~ The ~~increase of the~~ Small Incumbent Local Exchange Carriers' Basic Residential Service ~~Rate from \$20.25 to \$30.00, exclusive of other charges, will be achieved incrementally over five years commencing in 2015 at a rate of 20% per year.~~ Rates must be in a range of \$30, inclusive of additional charges, to \$37.00, inclusive of additional charges. This rate range of \$30.00 to \$37.00 will be presumptively reasonable and non-rebuttable. Actual rates will be set in the individual General Rates Cases of the Small Incumbent Local Exchange Carriers.

10. ~~8. Staff of the~~ The Commission's ~~Communications Division~~ staff will ~~develop and adopt~~ consider a set of factors - collectively agreed upon by parties - including the presence of anchor institutions, network redundancy, public safety, and service quality ~~that will be considered~~ when evaluating broadband-capable network investments during the Small Incumbent Local Exchange Carriers' ~~GRCs. Once developed, the Commission will use these factors to determine how much of the investment costs for deployment of broadband-capable facilities, that also support high quality voice communications, may be recovered by the Small Incumbent Local Exchange Carriers through ratepayers.~~ General Rate Cases. The Commission will continue to use the National Exchange Carrier Association Tariff No. 5 to encourage deployment of broadband-capable facilities as well as the current affiliate transaction rules.

~~9.~~ The Commission will continue to use the National Exchange Carrier Association Tariff No.5 to encourage deployment of broadband-capable facilities as well as the current affiliate transaction rules.

11. ~~10.~~ The advice letter filing date for the California High Cost Fund-A Program is changed from October 1 of each year to September 15 of each year.

12. ~~11.~~ As seven months of actual data and National Exchange Carriers Association data ~~is usually~~ may not be available until after September ~~15;~~ 15, the Commission's Communications Division will enter final calendar year ~~National Exchange Carriers Association~~ data upon eventual receipt. In lieu of the National Exchange Carriers Association data the Small Incumbent Local Exchange Carriers will enter placeholder National Exchange Carriers Association data with the submission of their September 15 advice letters, the Commission's Communications Division will then enter final calendar year National Exchange Carriers Association data upon receipt, for final analysis in a draft Resolution setting California High Cost Fund-A Program support.

13. ~~12.~~ In requesting regulatory changes for industry-wide effect the Small Incumbent Local Exchange Carriers will do all of the following: 1) Include cites that authorize the requested adjustment: the Commission Decision number and relevant page number or Federal Communications Commission Order with a copy of order and page reference. A copy of the cite is necessary in order to describe this in the resolution; 2) File Excel spreadsheet with detailed, traceable calculations showing each amount requested for each adjustment. The calculations will contain data in spreadsheet and not references to data that are not included in the provided spreadsheets, and provide link if/when necessary; 3) Insure that each adjustment request is itemized separately rather than combined into one total with other adjustments; 4) Insure that adjustment requests fall into the time frame of Commission or Federal Communications Commission decision(s) justifying the adjustment request and acknowledge that filed adjustments that are outside of the time frame will be returned to the carrier

for filing the next year. The above items are required for the Commission's Communications Division to accept and approve any adjustment. Adjustments not provided for as described above will be returned to the Small Incumbent Local Exchange Carriers for immediate correction.

14. ~~13.~~ All other requests and motions presented in Phase 1 of this proceeding are denied.

15. ~~14.~~ Rulemaking 11-11-007 remains open.

This order is effective today.

Dated \_\_\_\_\_, at San Francisco, California.

**ATTACHMENT A**

R.11-11-007: CHCF-A Review  
Procedural Change Recommendations for May 28-29 Workshop

R.11-11-007: CHCF-A Review  
Procedural Change Recommendations for May 28-29 Workshop

- Each Small ILEC will file an advice letter by September 15 of each year (rather than current October 1 requirement).
- Seven months of actual data and National Exchange Carriers Association (NECA) data ~~is~~ usually may not be available until after September ~~15;~~ 15. In that event, CD will enter final calendar year ~~NECA~~ data upon eventual receipt. In lieu of NECA data, Small ILECs should enter “placeholder” NECA data with the submission of September 15 advice letters, then CD will enter final calendar year NECA data upon receipt, for final analysis in draft Resolution setting CHCF-A support.

Carriers currently use a standard format for worksheets:

In requesting regulatory changes for industry-wide effect, Small ILECs would:

1. Include cites that authorize the requested adjustment: the Commission Decision number and relevant page number or FCC Order with a copy of order and page reference. A copy of the cite is necessary in order to describe this in the resolution;
2. File Excel spreadsheet with detailed, traceable calculations showing each amount requested for each adjustment. The calculations will contain data in spreadsheet and not references to data that are not included in the provided spreadsheets, and provide link if/when necessary;
3. Each adjustment request must be itemized separately rather than combined into one total with other adjustments;
4. Adjustment requests must fall into the time frame of Commission or FCC Decision justifying the adjustment request. Any filed adjustments that are outside of the time frame will be returned to the carrier for filing the next year;
5. The above items are required for CD to accept/approve adjustment. Adjustments not provided for as described above will be returned to Small ILEC for immediate correction.

**Cites from D.91-09-042 Attachment A**

*In each succeeding year, each rural and small metropolitan company shall file with the Commission an advice letter incorporating the net settlements effects upon such company of regulatory changes ordered by the Commission and the Federal Communications Commission (FCC). These advice letter filings will include the previously authorized annual filings for interLATA SPP to SLU shifts set forth in D.85-06-115 as well as all other regulatory changes of industry-wide effect such as changes in levels of interstate high cost funding, interstate NTS assignment, other FCC-ordered changes in separations and accounting methodology and Commission-ordered changes such as rate changes affecting access charges, intraLATA toll or EAS settlements revenues.*

*For those companies requesting CHCF support, the filing shall include, unless otherwise exempted herein, at least seven months of recorded data annualized for the year in which the advice letter is filed and adjusted for known Commission regulatory decisions regarding the utility’s rate of return.*



**General Rate Cases**

Carriers provide accurate estimate of bookings to Rate Base for December when providing initial nine 9 months actual numbers for their GRC. Usually there are large amounts booked to December which are known at time of sending in GRC Data.

**(End of Attachment A)**

Document comparison by Workshare Compare on Wednesday, December 17, 2014 12:42:45 PM

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